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HELPING AMERICANS PREPARE FOR RETIREMENT: INCREASING ACCESS, PARTICIPATION, AND COVERAGE IN RETIREMENT SAVINGS PLANS

HEARING

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HELPING AMERICANS PREPARE FOR RETIREMENT: INCREASING ACCESS, PARTICIPATION, AND COVERAGE IN RETIREMENT SAVINGS PLANS

THURSDAY, JANUARY 28, 2016

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, DC.

The hearing was convened, pursuant to notice, at 9:30 a.m., in room SD–215, Dirksen Senate Office Building, Hon. Orrin G. Hatch (chairman of the committee) presiding.

Present: Senators Grassley, Crapo, Cornyn, Thune, Burr, Portman, Heller, Scott, Wyden, Carper, Cardin, Brown, Bennet, Casey, and Warner.

Also present: Republican Staff: Sam Beaver, Professional Staff Member; Preston Rutledge, Tax and Benefits Counsel; Jeff Wrase, Chief Economist; and Marc Ness, Detailee. Democratic Staff: Joshua Sheinkman, Staff Director; Michael Evans, General Counsel; Kara Getz, Senior Tax Counsel; and Eric Slack, Detailee.

OPENING STATEMENT OF HON. ORRIN G. HATCH, A U.S. SENATOR FROM UTAH, CHAIRMAN, COMMITTEE ON FINANCE

The CHAIRMAN. The committee will come to order. I would like to welcome everyone to this morning's hearing on the ongoing effort to increase access, participation, and coverage of retirement savings plans. Financial security and retirement policy, in particular, have never been more important. Today, we will discuss policies designed to incentivize employers to set up retirement plans and to help employees save more for their retirement and make those savings last a lifetime.

When we talk about the status quo of retirement policy, there is both good news and bad news. The good news is that the private employer-based retirement savings system—particularly 401(k) plans and Individual Retirement Accounts, or IRAs—has become the greatest wealth creator for the middle class in history.

Under the current system, millions of Americans have managed to save trillions of dollars for retirement. In specific terms, thanks in large part to policies Congress has enacted over the years, American workers have saved more than $4.7 trillion in 401(k) plans and more than $7.6 trillion in IRAs.

Now, that is more than $12 trillion in total, more than double the amount workers had saved in 2000, despite the Great Recession, the market downturn in 2008, and historically low interest

rates since that time. Once again, that is really good news. But the bad news is that with the retirement of the baby boom generation, the fiscal pressure on public programs positioned to benefit retirees—programs like Social Security and Medicare—is growing exponentially, putting enormous strain on the Federal budget and driving the expansion of our long-term debt and deficits.

As this pressure mounts, participation in private retirement plans will be more and more important. Yet at the same time, as part of the constant drumbeat here on Capitol Hill for more revenue to pay for increased spending, some have proposed reducing the allowed contributions to 401(k) plans and IRAs. That, in my view, would be both shortsighted and counterproductive.

Over the years, we have learned that, for most American workers, successful retirement saving largely depends on participation in a retirement plan at work. Unfortunately, many employers, mostly small businesses, do not sponsor plans for their employees.

There are a number of reasons why an employer might opt to not offer a retirement plan, including cost, complexity, or administrative hassle. But whatever the reason, the result is the same. Fewer American workers are likely to save for retirement than would otherwise be the case.

As everyone will recall, last year, the committee established bipartisan tax reform working groups to examine all major areas of U.S. tax policy and identify opportunities for reform. One of those working groups focused specifically on tax policies relating to savings and investment. Today, the full committee will hear more about the various legislative proposals the Savings and Investment Working Group looked at as they considered options and produced their report.

I want to thank the two chairs of this particular working group, Senator Crapo and Senator Brown, for their efforts and their leadership on these issues. They looked extensively at a number of more recent proposals, and, like all of our working groups, they produced an excellent report. I look forward to delving more deeply into these issues here today.

Simply put, we need to do more to encourage employers who do not sponsor retirement plans to set them up. Toward that end, one of the first proposals described in the working group report would allow unrelated small employers to pool their assets in a single 401(k) plan to achieve better investment outcomes, lower costs, and easier administration.

This proposal for a multiple-employer plan, what some have called the, quote, "Open MEP," already enjoys bipartisan support here in Congress. Many of our colleagues have worked hard to develop and advance Open MEP proposals.

While I run the risk of missing some of my colleagues, I want to acknowledge the efforts of Ranking Member Wyden, Senator Brown, Senator Nelson—who has worked on this issue with Senator Collins on the Aging Committee—Senator Scott, and Senator Enzi, who held hearings on this MEP idea in the HELP Committee. And, as if that was not enough, just this week the Obama administration announced its support for the Open MEP idea.

Clearly, there is a lot of momentum for this proposal, which, in my view, is a good thing. Indeed, this is an idea whose time has

come. And while it is important to pursue policies to encourage greater retirement savings and investment, we must provide workers with the tools to ensure that their savings do not run out before the end of their lives. That is why I have put forward proposals to encourage individuals to purchase annuity contracts to provide secure, lifelong retirement income.

Today, there are obstacles in the law that discourage employers from adding annuity purchase options to their 401(k) plans and employees from purchasing annuities. We should do all we can to remove these obstacles, particularly given the decline of defined benefit pension plans in recent years.

Retirement policy has been an especially important topic here on the Finance Committee, and it has always been bipartisan. Indeed, most of the retirement legislation that Congress has passed in recent decades has been named for Senators from the Finance Committee, usually one from each party. I hope this will continue even during this election year, when attacks and accusations relating to retirement security, unfortunately, tend to gain a lot of traction.

I plan to do my part to ensure that the committee focuses on advancing policies that unite both parties. If we can do that, I think we can make progress.

I want to thank Senator Wyden for his great efforts that he has made since I have been chairman, and even before, to try to bring us together and have us do bipartisan work through this committee.

Before I conclude, I want to acknowledge that there is some interest in the committee in discussing the challenges facing multiemployer defined benefit pension plans and their beneficiaries. These are important topics that affect employers, workers, unions, plant managers, the Pension Benefit Guaranty Corporation, and, of course, current retirees who may be facing hardships.

They also highlight the challenge of delivering on the promise of lifetime retirement income and the stakes for retirees if the system fails. We certainly need to have a robust discussion of these matters in the committee, and I plan to convene a hearing on multiemployer plans in the next work period.

Today, however, I am hoping we can focus on bipartisan proposals to increase access to retirement savings plans. I am grateful to have Senator Wyden as co-leader of this committee. I am going to turn to him for his opening remarks at this time.

[The prepared statement of Chairman Hatch appears in the appendix.]

OPENING STATEMENT OF HON. RON WYDEN, A U.S. SENATOR FROM OREGON

Senator WYDEN. Thank you very much, Mr. Chairman, and I very much appreciate your desire to take this important area, once again, in the best tradition of the Finance Committee, which is to work in a bipartisan way. So I look forward to working with you and all our colleagues on it.

Over the last decade, policy experts and lawmakers have gathered in rooms like this to dissect the country's retirement savings crises again and again and again, and that includes a hearing held by this committee about a year and a half ago.

The numbers that underlie this crisis are jarring every single time I hear them, and our job is to make it different this time with meaningful legislation. Barely more than half of American workers have access to retirement savings plans through their employer. A middle-of-the-pack retirement account today is enough saved up to pay a 64-year-old retiree just a bit more than $300 a month. Half of accounts belonging to 25- to 64-year-olds have even less, and millions of American workers have no pension and nothing at all saved.

Despite those dire statistics, the nonpartisan Joint Committee on Taxation tells us that over the next 5 years, American taxpayers, the people we represent, are going to see more than 1 trillion of their dollars put into subsidies for retirement accounts. This is the second-biggest tax subsidy on the books.

The Congressional Budget Office, however, says that these benefits are disproportionately skewed to those who need the assistance the least. Less than 1 in 5 of those dollars goes to households with incomes in the bottom 60 percent of earners.

Minority Americans have it even worse. For young workers or people seeking jobs in restaurants, hotels, or construction, it may be nearly impossible to find an employer who sponsors a retirement plan with a matching contribution. And obviously, there are going to be great challenges with what is known as the "gig economy," which grows every year.

It is obvious that working families and the middle class need more opportunities to save, and, first and foremost, those are opportunities that ought to be available at work. Then the options that Americans have for saving need to better reflect the way people work and live in retirement. That means retirement savings built up at work have to be portable and provide meaningful lifetime income.

The good news is that steps are being taken now to create several new opportunities. In my home State of Oregon, we are one of three States that has passed what is called an "auto-IRA" law to cover those without employer-based options.

The bottom line for Oregon workers is going to be, when you get a job, you are going to get a retirement account, and you can begin to save. It will not be mandatory because workers can opt out, but it is going to relieve headaches and kick saving into a higher gear.

It was an important step for my State to take, because back in 2013, an AARP survey found that one in six middle-aged Oregon workers had less than $5,000 saved. A new report released this month from the Pew Charitable Trusts found that less than two-thirds of Oregon workers have access to retirement plans through their employers, and barely more than half have participated. But Oregon's auto-IRA plan, in my view, represents nothing less than a sea change in retirement saving.

I hope this trend leads Federal lawmakers to pass the President's national auto-IRA proposal. The administration has opened up what it calls "My-RA" plans to help workers nationwide get started with saving.

These smart new plans are aimed squarely at Americans with limited means who have been shut out of retirement. There are not any fees to eat into your savings, no minimum balances or con-

tribution requirements. You do not lose a penny that is put in. A very good way to build a nest egg.

Additionally, there are more proposals in the works that can make a big difference for a lot of Americans. Today, I am introducing a bill to strengthen the saver's credit so it does more for the people who need the most help. I note our friend, Senator Cardin, is here, and he has done important work on the saver's credit.

At a time when taxpayers are putting more cash into savings incentives that are skewed disproportionately to those who are best off, this proposal is a step that Congress can take to put a little more balance in Federal policy to ensure that all Americans have the opportunity to save and to get ahead.

As Senator Hatch noted, we have been working with a very large coalition of Senators, and particularly Senators Brown and Nelson on this committee, to expand retirement plans that bring together multiple-employers. Our proposal is aimed at getting the old rules out of the way, lowering costs, and easing the burden on employers.

So in addition to big progress with auto-IRAs and My-RAs, these are important pieces of legislation that will be coming up. Moving forward, we have an opportunity to address these issues in a bipartisan way.

Comprehensive tax reform, which we talk about in this committee and have for many months, has another opportunity for all of us. Bills designed to grow wages can make an enormous difference. And the recent turmoil in the financial markets is a keen reminder of why it is important to keep Social Security strong and reject calls to privatize that program.

One last point about the multi-employer pension crisis. This needs to be solved and soon. Congress passed a bad law over 1 year ago, a law that I opposed, and some retirees are looking at harsh cuts to the pension benefits they have earned. We must not let that come to pass, and we ought to be addressing that too in a bipartisan way.

Our challenge is to enact legislation as soon as possible, as well, to help the many coal miners in this country—and I appreciate Senator Brown's leadership on this issue. He has spoken about this repeatedly. Senator Warner cares about this as well. They deserve health and pension benefits that they earned over decades of back-breaking work.

The situation for mine workers gets worse with every passing day, and this, Mr. Chairman and colleagues, is another public policy emergency.

Mr. Chairman, thank you. We have a lot of colleagues who are interested in these issues and look forward to this hearing.

[The prepared statement of Senator Wyden appears in the appendix.]

The CHAIRMAN. Thank you, Senator.

Now, I would like to take a few minutes to introduce today's witnesses, starting with Dr. Alicia Munnell. Dr. Munnell is the Peter F. Drucker professor of management sciences at Boston College's Carroll School of Management, where she has taught for more than 18 years.

Before joining Boston College in 1997, Dr. Munnell was a member of the President's Council of Economic Advisers and also served as the Assistant Secretary of the Treasury for Economic Policy.

For the preceding 20 years, she worked at the Federal Reserve Bank of Boston, where she became senior vice president and director of research. She has received many awards, including the International INA Prize for Insurance Sciences and the Robert M. Ball Award for Outstanding Achievements in Insurance.

Dr. Munnell earned her B.A. from Wellesley College, her M.A. from Boston University, and her Ph.D. from Harvard University.

Our second witness will be Mr. John Kalamarides, who is currently serving as the head of institutional investment solutions and CEO of Prudential Bank and Trust. In his role, Mr. Kalamarides runs the Stable Value Institutional Retirement Income Institutional Fund and Prudential Bank and Trust, overseeing more than $260 billion in account values.

Prior to joining Prudential, Mr. Kalamarides was senior vice president of marketing and strategy for Cigna's retirement business. He has also held roles and led strategy projects for Accenture and Greenwich Associates.

Mr. Kalamarides is a graduate of Colgate University and earned a master's in business administration from the Amos Tuck School of Business Administration at Dartmouth College.

Finally, we will hear from Mr. Thomas Barthold, who is currently serving as Chief of Staff for our Joint Committee on Taxation. Mr. Barthold is no stranger here and is an indispensable asset on Capitol Hill. We all appreciate him on both sides of the floor.

He joined the Joint Committee staff nearly 30 years ago when he started as a staff economist in 1987. Over time, he worked his way to becoming Senior Economist, Deputy Chief of Staff, and Acting Chief of Staff until he assumed his current role in May 2009.

Prior to his arrival in Washington, Mr. Barthold was a member of the economic faculty of Dartmouth College. Mr. Barthold is a graduate of Northwestern University and received his doctorate in economics from Harvard University.

Also, I have asked Mr. Barthold to take a little more time during his opening than is customary to review some PowerPoint slides that outline several of the proposals analyzed last year by the Savings and Investment Tax Reform Working Group.

I want to thank all three of you for coming. This is a very important hearing.

I have to say that I have a number of commitments that I have to keep. I have two bills up in Judiciary. So I am going to have to go between here and the Judiciary Committee. So I hope it will not offend anybody, and we will keep this hearing going.

But I want to thank you all for coming. It means a lot to us. We will now hear witness testimonies in the order that they were introduced.

Dr. Munnell, please proceed with your opening statement.

STATEMENT OF ALICIA H. MUNNELL, Ph.D., PETER F. DRUCKER PROFESSOR OF MANAGEMENT SCIENCES, CARROLL SCHOOL OF MANAGEMENT, AND DIRECTOR, CENTER FOR RETIREMENT RESEARCH, BOSTON COLLEGE, CHESTNUT HILL, MA

Dr. MUNNELL. Thank you, Chairman Hatch, Ranking Member Wyden, and members of the committee. Thank you very much for the opportunity to testify today about helping Americans save for retirement and to talk about the Savings and Investment Bipartisan Tax Working Group report.

I would like to submit my written testimony for the record and then use my time to do two things. First, I would like to underline the importance of the issues that the working group addressed, and, second, I would like to argue that we are facing an enormous retirement income challenge and, therefore, we need even bolder changes.

Let me start by describing the retirement landscape to emphasize why this hearing is so important. My view is that the landscape is rocky, really rocky. We are facing a retirement income crisis. The center that I direct constructs a national retirement risk index which assesses the retirement readiness of today's working-age households. The index shows that about half of today's households are at risk of not being able to maintain their standard of living once they stop working.

The reason for this shortfall is twofold. We are going to need more money in the future for retirement, and, two, the traditional sources of income are providing less support than they have in the past. On the needs side, the major drivers are longer life expectancies coupled with relatively early retirement ages, high and rising health-care costs, and very low interest rates. On the income side, Social Security will provide less relative to pre-retirement earnings because of the rise in the full retirement age. In addition, high Medicare premiums and taxation of benefits under the personal income tax will reduce the net Social Security benefit.

The other major source of retirement income, the private pension system, is not working well. The typical working household with a 401(k) plan approaching retirement, somebody 55 to 64, has combined assets in their IRA and their 401(k) of $111,000. That may sound like a lot of money, but it produces only $400 a month in income. And those with coverage are the lucky ones. As the working group points out, about half of private-sector workers do not participate in any employer-sponsored plan at a given moment of time, and people simply do not save if they do not have an employer-provided plan.

The working group's report is aimed at primarily reducing the coverage gap and encouraging saving among lower-paid workers. The report discusses four main types of proposals.

First, several proposals would broaden access to potentially low-cost, multiple-employer plans by getting rid of the nexus requirement and the one "bad apple" provision. My view is that Open MEPs would be a useful vehicle for retirement saving provided that small employers are protected against high fees and unscrupulous actors.

Second, a group of proposals is aimed at small businesses, offering increased financial incentives to start new plans, additional incentives for auto-enrollment, and credits for contributions. My sense is that these proposals are positive, but I think they would have a relatively modest impact.

The third idea of providing coverage for long-term part-time employees seems to me like a great idea.

Finally, a proposal to enhance the saver's credit by increasing eligibility and making the credit refundable to retirement accounts could be extremely important. We have been doing a lot of work at the State level, and an expanded saver's credit could be a very helpful component of State auto-IRA proposals.

The working group should be commended for its proposals to expand retirement saving, and anything done in this day and age on a bipartisan basis is a wonderful thing.

That said, the return-on-income challenge is enormous, and the proposals, while positive, I think are modest. I think we need bold changes to solve this problem. Putting aside the issue of fixing Social Security, the two most important things that I think should be done are to make the 401(k) system work better and to enact Federal auto-IRA legislation.

Let me just say a word about each. 401(k) plans should be required to automatically enroll all workers, not just new hires, and the default contribution rate should be set at a meaningful level and then increased until the combined employee/employer contribution rate reaches at least 12 percent of wages. In addition, we need a more comprehensive approach to limiting leakages, and these changes would go a long way to making 401(k)s work better.

Automatic coverage. The working group recognizes the importance of the coverage gap, but I do not think financial incentives alone will solve the problem. We need to automatically enroll uncovered employees into a retirement savings program. As I have noted, many States are setting up their own auto-IRA programs, but 50 separate programs seems like a crazy idea to me. I think it makes much more sense to have such legislation passed at the national level.

In short, we have a really big problem, and, while the working group report is a step in the right direction, I think we need much bigger changes to fix the whole system.

Thank you.

[The prepared statement of Dr. Munnell appears in the appendix.]

The CHAIRMAN. Thank you.

Mr. Kalamarides, we will take your testimony now.

STATEMENT OF JOHN J. KALAMARIDES, HEAD OF INSTITUTIONAL INVESTMENT SOLUTIONS, PRUDENTIAL FINANCIAL, HARTFORD, CT

Mr. KALAMARIDES. Thank you, Chairman Hatch, Ranking Member Wyden, and members of the committee, for the opportunity to discuss the retirement challenges facing American workers.

I am Jamie Kalamarides, and I lead the investment businesses and trust business for Prudential Retirement. Prudential is the second-largest U.S. life insurer and a top ten global asset manager.

We provide retirement plans for all size corporations, governments, unions, and not-for-profits.

The primary focus of my testimony is expanding access to and participation in multiple-employer plans, a structure that enables small business owners to pool their resources into a single plan and thereby enjoy efficiencies typically limited to larger plans and to share those benefits with their workers. This topic is covered in more detail in my written testimony and our white paper, which I am submitting for the record, entitled "Multiple Employer Plans: Expanding Retirement Savings Opportunities."

[The white paper appears in the appendix on p. 47.]

Mr. KALAMARIDES. Retirement plan coverage is the critical gap in providing financial security to working Americans. According to EBRI, those with access to workplace-based plans save 16.4 times more than those without. Retirement plans are available at most medium and large employers, and, due to automatic enrollment, escalation, and default investments, they work, but only 50 percent of the 6.5 million small businesses with less than 100 employees offer plans. And this lack of coverage is especially acute for the 30 million women, 12 million Latinos, 6 million African-Americans, and 4 million Asian-Americans who work at these small businesses.

In 2015, Prudential surveyed 850 small businesses without plans and found that there are three barriers to adoption of plans: cost, administrative hassle, and fiduciary responsibilities. In the same survey, we found that demand for 401(k)s and multiple-employer plans would increase by 250 percent if we removed these barriers.

As recognized by the chairman, this committee's Savings and Investment Working Group, and most recently by the Obama administration, open multiple-employer plans can be an important part of the solution.

So to expand sponsorship and participation in Open MEPs, we recommend four changes in Federal law. First, remove the "commonality of interest" requirement and permit unaffiliated businesses to pool their purchasing power into a single plan.

Second, reduce the fiduciary and tax liability of small business owners to only those decisions that they make. Do this by removing the tax qualification provisions that hold the MEP and other participating employers potentially liable for the acts of others, and limit the fiduciary responsibility of employers to the prudent selection and monitoring of the MEP and forwarding timely contributions.

Third, establish a model MEP plan design that includes behavioral finance best practices and eliminates discrimination testing. This could be accomplished through legislation or direction to Treasury, IRS, and Labor.

Fourth, ensure that Treasury and Labor have the enforcement capability to protect small employers and their employees.

The benefits of these changes can be substantial. Employees without access will be automatically enrolled, save through institutional investments, and have the possibility of employer matches. Employers will have limited ongoing costs and administrative hassle. And with model plan design, competition will be based solely on investment, performance, service, and price. Small businesses

can switch providers easily, and enforcement may be easier. Finally, according to an ICI-Deloitte survey, all-in fees could fall by 80 to 100 basis points.

Open MEPs are supported by the U.S. Chamber of Commerce, AARP, the ERISA Advisory Council, the American Benefits Council, the Obama administration, and in every retirement coverage bill introduced in the 114th and the 113th Congresses, including bills by Chairman Hatch; Senators Collins, Nelson, and McCaskill; Senators Harkin and Brown; and Senator Whitehouse.

But access to workplace-based savings is not enough. With tens of thousands of Americans reaching retirement every day, workers are searching for solutions to help them manage investment and longevity risks. And by including guaranteed retirement income in 401(k) plans, workers can achieve better certainty and security. So we fully support proposals identified by this committee's Investment and Savings Working Group, including the portability of lifetime income, annuity safe harbor, and lifetime income disclosure.

Finally, we support three additional concepts, particularly for low- and moderate-income families: expanding the current safe harbor for automatic enrollment to 10 percent of pay; allowing long-term, part-time employees to contribute to their employer-sponsored retirement plans; and expanding the saver's credit to further encourage lower-income families to save for retirement. This could be especially powerful if that credit could be deposited as a match into an Open MEP.

Thank you, Chairman Hatch, Ranking Member Wyden, and the members of this committee and their staffs, for your focus on expanding retirement saving solutions at the workplace, especially through MEPs.

We look forward to working with the committee on these important issues. I will be happy to answer any questions you have.

[The prepared statement of Mr. Kalamarides appears in the appendix.]

The CHAIRMAN. Thank you. We appreciate your testimony.

Mr. Barthold, we are very interested in what you have to say, naturally.

STATEMENT OF THOMAS A. BARTHOLD, CHIEF OF STAFF, JOINT COMMITTEE ON TAXATION, WASHINGTON, DC

Mr. BARTHOLD. Thank you very much, Mr. Chairman, Senator Wyden, members of the committee.

The chairman asked me to review some of the material from the working group's deliberations, and I have done that in a series of slides that you have before you in JCX–4–16, and, if it is large enough, it is also up here on the screen.

Just by way of background, the emphasis is on defined contribution plans. I think it is important to note that "defined contribution plans" mean individual accounts that consist of employer and employee contributions, and the employee benefits from the investment returns. But in a defined contribution plan, the employee also bears the risk of those investments.

The code provides multiple types of defined contribution plans for employees of the private sector, public sector, and tax-exempt em-

ployers. Again, just by way of review, the defined contribution plan consists of elective contributions and employer matches.

On the side of this, outside of an employer plan, taxpayers generally, up to certain income limitations, may contribute to individual retirement arrangements. This is another form of a defined contribution retirement saving plan, and the IRA is also the basis of some employer-sponsored retirement plans that the Congress has created to try to spur maintenance of such plans by small businesses. These are the SEP, the simplified employee pension plan, and the SIMPLE IRA plan.

The reason the working group emphasized looking at these sorts of plans is in the next two graphs, where you can see, while total coverage of participants in some sort of employer plan in the private sector has been growing through time, the growth has all been in terms of active participation in defined contribution plans. In the second picture, you see the thick blue line climbing steeply to the right. The dashed green line tailing off is defined benefit plans. So, as Chairman Hatch noted in his opening statement, this is a fundamental shift in terms of how employers make opportunities for employees to save for retirement income.

A key point, as emphasized by both the co-panelists, has been employee participation and access to these plans in the private sector. Slightly less than half of employees participate in a defined contribution plan in any one year.

So what are the impediments? The working group identified access as a possible impediment; that not all employees may be covered; in particular, low participation rates; low contribution rates; and then, opportunities for use of savings before retirement, so that assets may be dissipated before they become available for retirement income, so-called "leakage."

So the policy goals identified by the working group are: how to increase access, how to increase participation, how to increase contributions, how to discourage leakage, and, to go to the point that the chairman noted, how to promote lifetime income once those assets have been accumulated.

I will skip over, for the most part, discussion of multiple-employer plans, the MEP plans. Mr. Kalamarides discussed that in quite a bit of detail. I will note that the working group reviewed several bills from the 113th Congress that would have provided some of the changes advocated by Mr. Kalamarides. As an additional note, they would not have provided a model safe harbor MEP and would not, at the same time, necessarily have included auto-enrollment, although other legislation that the working group considered looked at auto-enrollment.

What were some other problems identified by the working group that might contribute to a lack of access? Well, among small businesses, by scale, running a lot of employee benefit opportunities involves overhead for the business, and that is spread across fewer employees. So that means it is more costly per employee.

Under present law, there is a credit for small employer pension plan startup costs. There have been proposals put forth by members of this committee and elsewhere in the Senate and in the President's fiscal year 2016 budget that would increase the tax

credit available for startup costs, increasing the maximum amounts and the duration.

The President's proposal, as noted on slide 14, would provide a credit to an employer with an existing plan that added an auto-enrollment feature to its plan.

To get to auto-enrollment perhaps in more detail, this slide 15 highlights, I think, the key policy point that the working group looked at, and that is that the Congress has long had multiple policy goals in the retirement area.

One is to provide incentives to try to accumulate assets for retirement income, but to do that in a way that is fair, in a way that is, in the jargon of the industry, not top-heavy, a plan that does not just benefit the highly compensated employees of the employer.

So there are nondiscrimination tests. So, if you have an auto-enrollment plan with opt-out features, there is always a question of, do you fail the top-heavy test, the nondiscrimination test?

Under present law, there is a safe harbor that sets up a default rate of not less than 3 percent, but not more than 10 percent. Some of the proposals reviewed by the working group, S. 1270, S. 1970, would increase those default rates that qualify for the safe harbor, saying that if you meet these safe harbor tests, you do not have a discriminatory plan. Also, there is a credit for small employers provided under S. 1270 and S. 1970, again, to try to encourage startup contributions by employees.

Another factor in terms of nondiscrimination testing that may have impeded participation and the offering of plans by some employers, is what to do about part-time employees. If part-time employees do not contribute, you might run afoul of the nondiscrimination rules. For this, among other reasons, the code and ERISA, under present law, allow certain employees to be excluded.

With growing use of part-time employees, but part-time employees who may be long-term employees, H.R. 2117 and the President's fiscal year 2016 budget proposal were reviewed by the working group, because these proposals would define a concept of a long-term part-time employee and allow a plan to include those individuals and not run afoul of nondiscrimination tests otherwise applied.

Under present law, we have also, as Professor Munnell noted, a saver's credit. There were several proposals reviewed by the working group that would increase the value of the saver's credit and make it refundable. By way of review, the saver's credit is targeted at trying to generate asset accumulation by lower-income taxpayers.

The last point identified is sources of leakage and maintaining lifetime income from assets accumulated. The Congress has provided exceptions to the 10-percent penalty for early distributions. For example, Congress has provided for hardship withdrawals for immediately needed funds.

While not required, many plans offer loan options. And the working group found that the inability to make timely repayment of loan balances may diminish retirement funds when the employee reaches retirement age or take accumulated funds out of retirement solution if the employee changes jobs.

For that reason, the working group reviewed S. 606, and this is a proposal that would extend the time for rollover of loan offset amounts to not let accumulated assets fall out of retirement solution when an employee either retires or changes jobs. It would also limit certain types of loan programs to essentially try to discourage what some have viewed as credit card-type loan arrangements that are offered by some employer plans.

Looking at slide 22, let me just review the basic difference here. The classic defined benefit plan always has to provide an annuity option. It is rare for a defined contribution plan to provide an annuity option. Some plans do provide, within defined contribution plans, annuity vehicles that can be purchased, but if you change employment, you may not be able to take that vehicle with you to a new plan.

If the employer changes the plan, it might cancel out the annuity plan, and you lose that annuity feature. And so, in order to preserve that, the working group, again, looked at some proposals that would limit such possibilities, such as S. 1270 and the President's fiscal year 2016 budget proposals.

I have taken far more time than is probably warranted. My colleagues and I are always happy to answer any questions that the members might have.

I hope this brief run-through of the working group's deliberations has been helpful to this hearing.

[The prepared statement of Mr. Barthold appears in the appendix.]

Senator Scott [presiding]. Thank you, sir.

Senator Wyden?

Senator WYDEN. Thank you, Senator Scott.

We have had an excellent panel, three veterans in these important issues.

Mr. Barthold has scored three of my tax reform proposals, I believe, over the years, and I think, suffice it to say, my view on tax policy is, you want to give everybody in America the opportunity to get ahead. That is not penalizing success. That is about what makes America great because of our inclusiveness. My concern is that we are missing the boat with respect to that kind of spirit on savings policy.

At the last Finance hearing on retirement savings, the Government Accountability Office released findings that about 9,000 taxpayers, some of whom were able to do this with inside information, had over $5 million in their IRAs in 2011. More recently, there have been press reports of executives with Roth IRAs with balances over $30 million and over $90 million. When you are talking about Roth IRAs, that money is not going to be taxed.

My concern is, we want everybody to get ahead, but we want a policy in the savings area that, in my view, really is not as out-of-whack as what we have today. I mean, you have the American tax code letting some of the most affluent Americans shelter millions of dollars while providing little incentive for most Americans to save.

That is out of whack, and I would like to change it.

Dr. Munnell, you have done a lot of groundbreaking research in this area. What kind of recommendations could you give the com-

mittee to reform savings policy to give everybody a chance to get ahead, for the kind of inclusiveness that I have described, particularly when, this spring, the public and this country are going to put more than $1 trillion of their money into subsidies for these accounts? What can we do to get more balance, Dr. Munnell?

Dr. MUNNELL. Senator Wyden, my main message is that there should be a mandate in this country so that every employer puts their employee into some type of retirement plan and that employee has the right to opt out.

So I am very big on the notion of bringing everyone into the tent. I am not so sure what I would do with the sort of egregious amounts in some of the IRAs and some of the Roth IRAs. I do not like to see the tax shelters abused, actually, by very wealthy people. I would tread carefully, though, in terms of setting limits.

Senator WYDEN. That is why I asked you, because I want you to help us tread carefully so that you basically wring the maximum value out of this enormous sum of money.

Dr. MUNNELL. So I would bring everybody in. I would look very carefully at these people who have the huge balances and try to figure out exactly how they got there.

I would move slowly before I just impose caps on——

Senator WYDEN. We have been moving slowly on this now for a couple years. And I did not use the word "cap" either. I want to ensure that everybody has a chance to get ahead.

Dr. MUNNELL. Yes.

Senator WYDEN. Mr. Kalamarides, if I could, the new economy—and Senator Warner has done a lot of good work in this area—what it comes down to, for me, is that ERISA just really has not kept up with this very different world.

In the 2016 economy, we have workers carrying more of the load in the shift from defined benefit to defined contribution. We have a much more diverse workforce, more part-time workers. Gone are the days of the gold watch at the end of a 40-year career with one company.

I would be interested, because you all do a lot of work in these precincts, what kind of ideas do you think would be most attractive to, in effect, update our retirement policies from an ERISA law that is 40 years old?

Mr. KALAMARIDES. Thank you, Senator Wyden.

I want to acknowledge the importance of expanding access and availability for long-term part-time workers. Many of the workers in the gig economy derive some of their income from long-term part-time work, and, if we can expand that availability and participation at their workplace, they will have a place to save.

In addition, many of these workers work at small businesses that do not offer retirement plans. Let us offer open multiple-employer plans and reduce the barriers that I addressed earlier, allowing unaffiliated businesses to pool their purchasing power; transferring the liability from small business owners to professionals, not eliminating the liability, so we still protect those workers; removing the one bad apple rule; and adopting a model plan design.

This is especially important for workers who move between employers. If they happen to be working in that same group of employers that all participate in that employer plan, they do not have

to transfer their assets. We do not have the leakage that we have talked about earlier from rollovers.

Then finally, for those who are entirely dependent on the gig economy, those who are self-employed, IRAs and HRAs are an effective way to help them save. We do not want to have the unintended consequence of making them employers along the way. Let us expand Open MEPs, let us expand long-term part-time workers.

Senator WYDEN. I want to ask you to answer something in writing, Mr. Kalamarides. Senator Scott and I were just whispering that we are both interested in the portability question. So I will wait for Senator Scott's question.

But we have really tried in the health care area to also drive something that reflects a modern economy. We created a health care system after World War II that was completely tethered to the employer, and that was because we had to.

Now, we are going to have more options. Yes, employer-based coverage, but also other options to do what you have to do to have some additional opportunities for portability.

So Senator Scott and I will work with our colleagues on a bipartisan basis on that one.

Thank you, Mr. Chairman.

Senator SCOTT. Senator Brown?

Senator BROWN. Thank you, Mr. Chairman. Thank you to Senators Hatch and Wyden for their work on this for this hearing.

I am grateful particularly to Mr. Barthold for his patience and his wonderful explanations during some of these working groups. I think the idea that Senator Hatch had of these working groups makes so much sense. I think it demonstrates that if the committee focuses on discrete areas of the tax code, we can achieve bipartisan agreement on narrow, concrete proposals. That is what we were able to do with tax extenders. It is what Senator Crapo and I, I believe, achieved in this working group.

The comments that all three of you made speak to the seriousness of how hardworking Americans face such an uncertain future. It is beginning to be understood increasingly by people here what people at home have understood for years, that whatever they have in savings—and the fact that they do not have a defined pension benefit—is almost always very, very inadequate and that that is going to matter.

We have seen, particularly, as union membership has declined, so has access to these plans. We have a defined contribution system that works well for higher-income workers but too often leaves behind low-income workers who have suffered from stagnant wages for most of the last 20 years to begin with—nothing new, given the expertise that the three of you have.

The Federal Reserve's Survey of Consumer Finances reports that the median retirement account balance among households on the verge of retirement is $14,500. Imagine that. I mean, we sit here with good-paying jobs around this table, we sit here with a good defined pension benefit, we sit here, most of us, with adequate or way more than adequate savings, and we do not, as President Lincoln said, get our public opinion baths often enough to hear that that number is very real to so many people, that $14,500.

There are three things we can do. I want to say a few words and then ask you a question, Mr. Kalamarides.

We must address the retirement emergencies poised to devastate far too many workers. I will talk about that in a second. Second, we should implement a number of the common-sense bipartisan reforms that Senator Crapo and I recommended, including one our working group discussed and came to some bipartisan agreement on, with legislation to make it more attractive to convert to employee stock ownership plans. These companies help all workers at a company build wealth and enjoy a much more secure retirement.

Just this week, I talked to people from Messer, a major construction company that has been an ESOP for 30 years in southwest Ohio. Much beyond that, I have been to visit a company called Lifetouch in Galion, about 10 miles from where I grew up, Galion, OH, that does school pictures, and they are growing and growing and growing. It has been an extraordinarily successful ESOP.

I also met with someone from Amsted Industries out of Chicago which does manufacturing, including in my State, heavy manufacturing, and has helped a lot of their workers not just to have middle-class standards of living now, but well into the future.

Finally, we need to expand Social Security—I know you are doing some work on that in Boston—and reform our system with tax incentives for retirement to ensure that workers have access to tax-preferred retirement savings and annuitized lifetime income.

Before the committee addresses any of these issues, though, I want to talk about something that I know matters to Senator Warner, Senator Casey, Senator Cardin, and Senator Portman, at least us. Senator Wyden has been very outspoken on it. Senator Hatch has supported it. That is, what we do about these pension systems. Starting with Central States, Senators of both parties have mentioned this legislation that is well-intentioned but cannot realistically pass this Congress. I am willing to work with any colleagues interested in putting together a bipartisan comprehensive effort.

Second, this committee must immediately address—and that is what Senator Wyden talked about earlier, and I know the interest of Senator Warner in this—the emergency confronting 125,000 coal miners and their families. Through no fault of their own, these workers are at risk of spending their retirement in poverty if the retirement plan fails, as it is projected to do by 2017.

Senator Hatch has made supportive comments, as have others on this committee. If the plan fails, it will be taken over by PBGC, and, unfortunately, PBGC is already stretched, in terribly dire condition, with a total deficit of some $62 billion. If the mine workers' pension fails and the plan is taken over by PBGC, you have to think the future of PBGC is not so good.

That is why we should not go down that road. This committee should act on the bipartisan legislation coming from the two West Virginia Senators.

So my question—and sorry for the early comments about other things—but my question, Mr. Kalamarides, is, our working group recommended a number of important issues that we came together on, and I think there is real potential for Congress moving on this and this committee moving on this, including the open multiple-employer plans, as you know.

Tell us about the population that would be affected by this. How many workers? What do their demographics look like? How much do they make? Where do they live? What kinds of businesses and business owners would be able to offer plans? Talk that through. That is my only question.

Thank you.

Mr. KALAMARIDES. Thank you, Senator Brown, for both your leadership on the Investment and Savings Working Group and your advocacy for open multiple-employer plans.

Open multiple-employer plans can serve small businesses, in particular. There are 5.6 million small businesses that employ fewer than 100 employees. They employ 55 million American workers. Of those 55 million American workers, 30 million are women, 12 million are Hispanic-Americans, 6 million are African-Americans, and 4 million are Asian-Americans.

They tend to earn less than those who are at medium and large employers. Fifty percent of these small businesses do not offer plans. An open multiple-employer plan, by allowing small businesses to pool their purchasing power, removing the one bad apple rule, and transferring that fiduciary responsibility to professionals, will allow those small businesses to offer retirement plans.

We see the take-up rate increasing by 250 percent if we can pass these changes, and, therefor, we believe that all these working Americans can improve their savings and take advantage of the ERISA environment that we have described that gives good protections. And with automatic enrollment, automatic escalation, and lifetime income, they can enjoy financial security.

Senator SCOTT. Senator Thune?

Senator THUNE. Thank you, Mr. Chairman. And thank you to members of our panel for being here. This is an opportunity, I think, to explore numerous proposals that have been advanced to expand opportunities for Americans to save for retirement. It is something that really ought to have, I hope, broad bipartisan support.

I want to commend Senators Brown and Crapo for their efforts as co-chairs of the Savings and Investment Working Group last year, and I hope that this committee will provide an opportunity to further examine many of the proposals that were discussed in their report.

I would also recognize and thank Mr. Barthold, for he and his staff did a lot of the heavy lifting on all those working groups. So we appreciate what came out of that. I think there is a lot of food for thought and hopefully, ultimately, more than that, but also action when it comes to making a lot of reforms to our tax code that will generate more growth in our economy and, hopefully, with regard to this specific issue, encourage people to save more for their retirement.

I know this question has sort of been touched on already, but there has been a proposal to increase the amount of the existing credit offered to small employers who start a qualified retirement plan. Both Chairman Hatch and President Obama have suggested that the credit should be substantially increased beyond the current $500 amount. Now, unfortunately, the use of this credit has been very, very weak.

So my question is for anyone on the panel. Do you believe that increasing the amount of this credit would also increase the number of small businesses that take advantage of it, and is this something that Congress should consider if and when there is a retirement tax package?

Dr. Munnell?

Dr. MUNNELL. In this nice collegial environment, I hate to be negative, but my gut is that increasing that credit from $500 to $1,500 is really not going to have a very big effect. So it is not going to hurt anybody, but I do not think you will see that much more take-up.

There are just a lot of barriers standing in front of small businesses in terms of their ability to set up plans.

Senator THUNE. That is not one of them.

Dr. MUNNELL. Yes.

Senator THUNE. Mr. Kalamarides?

Mr. KALAMARIDES. I think that an expanded tax credit for small businesses in conjunction with the changes that we have talked about for open multiple-employer plans will increase the take-up rate among small business owners.

For small business owners, three barriers that have been identified by the Savings and Investment Working Group, the GAO, and our studies suggest that cost, administrative hassle, and fiduciary responsibility are the big challenges.

The proposals that the Savings and Investment Working Group suggested around Open MEPs help on the ongoing administration of the plan. Getting small businesses interested in adopting an expanded tax saver's credit would assist in setting up payroll changes and lowering some of the fixed costs that cannot be shared with other employers.

Senator THUNE. One area that has not received as much attention—and I know it has been touched on already here today—deals with part-time employees in the retirement area. We know that more and more Americans are employed part-time. People are taking part-time work either by choice or by circumstance, and typically these employees do not have access to retirement plans at work.

In your experience, what are the challenges to getting part-time workers covered? I think Senator Wyden already touched on this a little bit. But is there anything that can be done to expand access to retirement plans to put more part-time employees in those plans?

Mr. KALAMARIDES. The Savings and Investment Working Group made the proposals, and we support them, to help expand long-term part-time workers' access to and participation in defined contribution plans.

Currently, only 30 percent of part-time workers have access to defined contribution plans, and the situation is worse at small businesses: less than half of them even offer a retirement plan to all workers. So long-term part-time workers, often with two jobs, in low- to moderate-income families, can and do save, but what they are managing is income volatility, and they lack access to lower-cost investment solutions.

Open multiple-employer plans, in conjunction with changing the rules and allowing long-term part-time workers to save at their place of employment, will help them save and achieve financial security.

Senator THUNE. Mr. Barthold, as we encourage more Americans to save for retirement, that certainly applies when you have more low-income earners who may find it more difficult to save.

There has been a proposal to make the existing small saver's credit refundable. As you know, refundable credits, such as the EITC, historically have had a much higher rate of fraud and error than nonrefundable credits, and it is generally understood that when Uncle Sam is sending out checks, it has the unfortunate effect of encouraging bad actors.

Would you agree with that general point regarding refundable credits, and if so, before Congress considers making the small saver's credit refundable, are the prospects for increased fraud and error something that we need to take into consideration?

Mr. BARTHOLD. Senator Thune, the members are always concerned about the ability of the IRS to administer and taxpayers to comply. As you note, there is evidence that existing credits and refundable credits have been a source of compliance issues, but beyond that, really any sort of refund—it does not have to be refundable credit-generated—is the target of fraudsters.

The refundable credit may magnify that. But yes, certainly, our staff would work with the Finance Committee in terms of design to ensure that you are comfortable with the ability of the IRS to administer it and with compliance rates with any new provision that you might consider.

Senator THUNE. Thank you, Mr. Chairman.

Senator SCOTT. Yes, sir.

Mr. Kalamarides, a couple questions for you. Number one, in South Carolina, the average person around the age of 65 has less than $50,000 in liquid savings and less than $100,000 in their retirement account. This is pretty consistent, I am sure, throughout the country, but South Carolina seems to be in a particularly poor position for retirement.

My question is, as you think about that group of retirees who are very close to looking for alternatives and, at the same time, the new workers who are coming into the workforce, many of those folks will have seven different jobs during their lifetime of work. Therefore, the Open MEPs may be an opportunity to discuss portability, and, Mr. Barthold, I would love to hear your comments on how we make portability easier for the average person to understand and appreciate.

My final question is, when we are thinking about small business owners, having run a business for the last 15 years before I was elected to Congress, one of the things that is not necessarily on the top of our list is expanding benefits when we are seeing a contraction in the economy. So how do we make the conversation more important, and, frankly, how do we make the information more readily available, because I think that is a major part of the conversation that seems to be lacking?

Mr. KALAMARIDES. Thank you, Senator Scott.

I would agree with your concern about access to liquid assets and retirement, the concern that employees and citizens have about retirement savings. This week, the Center for Enterprise Development, CFED, published their annual report and said that 43.5 percent of Americans do not have 3 months' worth of salary available to cover emergency expenses.

So savings at the workplace and for retirement is absolutely critical. And with portability, the first issue you raised, Open MEPs can help. When multiple-employer plans are organized on a geographic basis and an employee moves from one employer to another, even for those employers who may not be affiliated, they do not need to switch their plan. They do not need to roll over their plan. They can stay enrolled.

Moreover, if there is a model plan design at the Federal level, all the plan designs will be similar between any multiple-employer plans. Individuals switching from one to another will not have to worry about undue changes in the rules. Service, investments, and price may differ and service providers may differ, but that will help on portability.

One other important thing about portability that the Savings and Investment Working Group specifically addressed was around lifetime income solutions, and we agree with the Investment and Savings Working Group's proposal to make changes to allow lifetime income solutions to have more portability if an employer or if a provider decides not to offer it anymore, to allow a rollover out. We agree with the Investment and Savings Group recommendation on that.

Senator SCOTT. Mr. Barthold, do you want to comment on the portability? And frankly, could you comment on the leakage as well, while you are starting your comments on portability?

This 59-day window, how much does that play into the leakage concerns that we have? If you would talk first about portability, that would be great.

Mr. BARTHOLD. Thank you, Senator Scott.

I think it is important to remember that a lot of the growth in defined contribution plans and popularity with employees of defined contribution plans is because they are portable. The problem with defined benefit plans, from an employee's perspective, is that you could have left one employer at age 30, and the benefits would have been locked in at the nominal dollar value of 5 years of service at age 30 and you did not have the benefit of growth in that through time.

With a defined contribution plan, you can roll it into an IRA, you can often roll it into another employer's plan, and you can continue to participate in the growth of the economy through your investment.

So defined contribution plans inherently offer portability.

Employees' elective deferrals are always vested, always portable. The same is true of an employee's after-tax contributions, if there are after-tax contributions. Members may have a question about vesting requirements of an employer's match in terms of portability in defined contribution plans. That might be an area that members might want to explore.

Again, remember also, since an IRA is a defined contribution-type plan, it is ultimately portable. So, for a self-employed person who contributes to an IRA, everything is always portable as they move from opportunity to opportunity.

The working group, as you alluded to, had noted that there are possibilities for leakage. Sometimes human nature perhaps takes over and people say, "Oh, I am cashing out of my DC plan." Rather than rolling it over, I do not know, maybe they want to buy a sailboat to use Charleston Harbor because that looks good at the time.

Senator SCOTT. There are a lot of sailboats there, that is for sure.

Mr. BARTHOLD. We do have the penalties for early withdrawal. That is to discourage that sort of behavior. But the working group did examine other possible penalty-free withdrawals and the loss of assets to retirement solution at rollover opportunities.

But inherently, the defined contribution plan is sort of the ultimate portable vehicle in terms of accumulating retirement assets.

Senator SCOTT. It does not appear that the leakage can be stopped by the penalty. I think the penalty is 10 percent plus ordinary income, and looking at the number of folks who have made distributions from those qualified plans, perhaps they do not understand and appreciate the impact of ordinary income on the dollars that they take out.

Thank you very much.

Dr. MUNNELL. Could I just say a word about leakages, generally, because that is a very important problem in the whole retirement system?

Senator SCOTT. Yes.

Dr. MUNNELL. We estimate that 1.5 percent of assets leak out each year. That does not sound like a very big number, but that means that assets at retirement are 25-percent lower than they would have been anyway, and when people do not roll over their accounts, they leak out through hardship referrals.

They leak out a little bit through loans, and they leak out because people can have access to their money at 59½. But fixing this inability to take your money when you move from one job to another would be enormously helpful.

Senator SCOTT. Thank you very much.

Senator Warner?

Senator WARNER. Thank you, Mr. Chairman. I want to thank Senator Hatch and Senator Wyden for holding this hearing. Great presentations by the panel.

Mr. Barthold, thank you again for, in these complex areas, helping us understand them in a rational way.

I want to make a comment first, adding to what Senator Brown spoke to, and Senator Casey I know is interested as well. We have 125,000 Americans, miners, many of them dependent upon the UMWA 1974 Pension Fund. That fund is about to go into dramatic arrears, and, as Senator Brown said, simply turning this over to PBGC is not going to be the right option.

We all have human cases on this. We had recently Mr. James McCoy, a miner from Wise County, 26 years worked in a coal company, retired. He already had a heart attack. He has esophageal cancer right now. He and his family are terrified about what hap-

pens when this pension fund, in effect, goes away or the benefits get cut dramatically.

I appreciate Senator Wyden and Senator Hatch and others saying there is a way that we can come in and fix this. The sooner we get at it, the better for a whole lot of mine workers who, through no fault of their own, are about to lose a set of benefits that they are completely dependent upon.

I also want to take a moment—and Senator Wyden has raised this issue. It is one that I have spent the last 10 months working on outside the day-to-day notion, and that is the kind of evolution of work as broadly based.

More and more, work is no longer based upon employment in an individual firm—and Senator Scott mentioned you are going to change jobs seven times. I think it will actually be exponentially higher, and, in effect, work is being broken into more and more discrete tasks and being bid out on a regular basis in terms of taskers, the gig or on-demand economy.

But if we step back a bit, we have already seen freelancers or contingent workers up about 35 to 40 percent of the workforce. We have just seen some recent data on the on-demand economy. That shows that literally 22 percent of Americans have offered an on-demand service. Now, these are folks who responded to an online survey, so there was some self-screening. And 44 percent of Americans have utilized an on-demand service.

I can tell you, this is only going to be an area that is going to exponentially grow. While there is great flexibility and freedom for folks who are working in this sector, there is no social insurance at all. And we are kind of caught up, I think, in a 20th-century conversation where we have this binary choice between 1099 and W–2.

We will have that debate, but in many ways, that legal distinction between an employee and any kind of contractor, I think, is precluding some of the new platform companies, who, I think, in many cases, may choose to do the right thing, but cannot do the right thing because of this legal battle on 1099/W–2.

Increasingly, I think you are going to see workers not just have multiple jobs over their careers or provide multiple services, but have multiple streams of income coming in at the same time as they patch together a series of work. We have talked about small employer plans, but we are going to see more and more often the individual as, be it he or she, in some notion, an independent entity on their own.

We have the IRA-type accounts. How do we think more expansively? I would like to hear the whole panel here—obviously, we need to be bolder. We think, in a sense, of the social contract for the gig economy in terms of retirement savings. How do we allow firms, without getting into the 1099/W–2 battle, to make contributions?

Is there an hour bank concept that can be dusted off and made relevant in the 21st century? How do we build further on portability? And I would love each of the panelists to address this issue.

Dr. MUNNELL. For people to have any sense of a secure retirement, they need to have a Social Security benefit as their base,

which means that the earnings that they earn over their work time have to somehow be credited to Social Security through a payroll tax on that. If you do not have that, then you are really starting out behind the eight ball.

In addition, people absolutely do not save on their own. They really do not. The only way they save is if they have an automatic savings mechanism that forces them to put some money aside each month. They also do save through their home by paying down their mortgage.

So everybody has to both have a way to get their earnings counted toward Social Security credits, and everybody who is working needs to have some automatic savings mechanism so that they have some supplement to Social Security going forward.

Senator WARNER. And that needs to be regardless of how many income streams they have going.

Dr. MUNNELL. That is right.

Senator WARNER. Please, very briefly, the last two.

Mr. KALAMARIDES. Senator Warner, I would agree with Dr. Munnell that Social Security has to be the base for our social safety net system and that payroll-based deductions are the most effective way for individuals to save.

I would categorize those working in this new economy in two categories: those who are entirely dependent on the new economy, entirely dependent on being an independent contractor, self-employed, and those who do that part-time and work maybe part-time long-term in another workplace. For those who work in that latter category who have part-time long-term employment at another workplace, I would like to agree with the Investment and Savings Working Group proposal to expand access to those workers to be able to participate in retirement plans at small businesses and Open MEPs to allow them to save at the workplace and get all the benefits that we have been talking about.

For those who do not, which I think is a smaller amount now, who are 100-percent dependent on the gig economy, there are two significant tax-deferred ways to save: an individual retirement account and a health savings account.

A single worker making less than $117,000 could save $5,500 per year in an IRA and $3,350 in an HSA. If the worker is over 55, they could save $6,500 and $4,350, respectively, even more if they have a family. Moreover, the saver's credit applicable for an IRA can be applicable to them as well.

These solutions can be solutions. I think that we do need to think about them specifically for the gig economy.

Senator SCOTT. Senator Casey?

Senator CASEY. Thank you very much.

I wanted to, first, start with the premise which I think is probably self-evident, but we need to remind ourselves of a couple of what I consider realities for the middle class and a huge segment of the American people.

Number one is, we have this strange disconnect between the data on the business page looking a lot better, unemployment cut in half in the last couple of years, by one estimate, 14 million jobs created, the stock market, despite some difficulties this year, way up from where it was. So all the economic data, or most of it, looks pretty

good, and yet all the other information about people's sense of the future, their belief that their children will do better than they will do, is way down.

So all of those indicators are bad. There are a lot of reasons for that, but lack of wage growth is one of them. We have had horrific wage growth over 40 years; we know that. But one of the drivers of this—call it what you will: pessimism or a sense of insecurity or anxiety—one of the driver's, of course, is what we are here to talk about today.

It is a crisis. The sense that people have—they do not have retirement security, they do not have the kind of security they would like—one of the ways to address that is by having this hearing and focusing on these broad issues, but at the same time, we have to work on issues that are right in front of us.

Senator Warner, Senator Brown, and others have focused on something that is an issue we can deal with right away, and that is the 120,000 to 125,000 coal miners, retirees, I should say, who are depending on us to get the job done to pass the Miners Protection Act.

So that is both a preventable problem, as well as a problem that would have a devastating effect on those families if we do not get it done. So we can prevent that horrific outcome if we work together. I do want to thank Senator Wyden and his staff for their continued work and interest in these issues. The issue of retired miners is something that I have worked on with the ranking member and a number of our colleagues for several years.

So that is something we can do right away.

Doctor, I think I will start with you, and I may only have time for one or two questions. The basic question I have is, can you itemize for me—itemize for us—a list of the best tools available to give families the best opportunities to save?

I outline that question, because as you testified to, less than 50 percent of private-sector workers participate in retirement plans. That is a stark number. And you also said 53 percent of households as of 2013 may be unable to maintain their standard of living in retirement, and this is an increase of more than 20 percentage points from a little more than 30 years ago.

So with that data, can you itemize for us the best tools? And some of this, I know, is by way of reiteration, but I think it is important to remind us what that list is and what the best tools are.

Dr. MUNNELL. I think the thing to keep in mind is that people, left on their own, are not going to save. That is why we have the Social Security system, and that is why we have employer-based retirement plans.

So to me, it is very simple: we need to fix Social Security. We are not going to do that today. People need that as a base for retirement income.

Then everybody needs access to a retirement plan through their workplace, and they need to be automatically enrolled in that plan, always with a right to opt out. But nobody goes out and sets up an IRA. There are trillions of dollars in IRA accounts, but most of that comes from rolling over money from 401(k)s and some from DBs. So people just need to be put where they should be and then given the freedom to move from there.

So for the uncovered, we need to put them into something, and that is what the States are doing. They are going ahead and doing it. And then we need the 401(k) system to work really well, because it is here to stay. We are not going back to DBs. And there we need to have automatic enrollment.

I know that the Pension Protection Act encouraged automatic enrollment, but it is not as pervasive as you think. If I were you, I would pass a law that says if you want to be a 401(k) plan, you have to automatically enroll all your employees in it every year and have the default contribution level be at 6 percent and automatically increase that level over time, and, of course, people can opt out of that.

But everything needs to be automatic if people are really going to end up with significant amounts of money at retirement.

Senator CASEY. In the interest of time, I will have our witnesses submit something for the record, if that is okay.

Thank you, Mr. Chairman.

Senator SCOTT. Yes, sir.

Senator Grassley?

Senator GRASSLEY. My first question will be to Mr. Barthold. By the way, I did not hear the testimony of any of you because I was chairing the Judiciary Committee. So please forgive me.

One policy goal identified by our Investment Working Group is preventing leakage, which refers to individuals depleting their nest egg prior to retirement. That is a real concern and something the committee has long sought to limit. However, as noted by the Joint Committee on Taxation, quote, "Restrictions on access to tax-favored savings before retirement may discourage individuals from making contributions."

So to you, sir. Are there any insights that you could provide for this tradeoff that may be helpful for the committee in evaluating policy proposals in the area of leakage?

Mr. BARTHOLD. Well, thank you, Senator Grassley. You quoted material that my colleagues put together, and the quote that you read was to flag the design issue that you and your colleagues always face: that we offer an encouragement to do a certain type of saving. We can make that more attractive if we make it more flexible.

One of the ways that Congress has chosen to make it flexible has been to allow certain exceptions for hardship withdrawals or reductions in penalties for certain favored uses. That can be attractive in leading to ultimately greater accumulated retirement savings, if people never exercise those options but contribute money with the knowledge that, yes, maybe I can tap into it if needed. It does have the downside of, when they draw on it—the point that Professor Munnell made just a few moments ago—you can have substantial loss of retirement assets.

I do not think that there is present a lot of good, empirical research that would allow us to pick and choose and say that certain existing exceptions from the penalties for early withdrawal should be repealed—that accumulation would benefit from eliminating those exceptions or not. It is an area where perhaps Professor Munnell might have some more insight from some of her recent work.

Senator GRASSLEY. Any one or all of you, I have a question about part-time employees. One policy option has been discussed: increasing employee coverage and mandating employers to allow long-term part-time workers to participate in employer-sponsored retirement plans. Before this committee considers such a proposal, I would like to better understand the barriers that currently stand in the way of more employers voluntarily offering such a benefit.

So my question is kind of a wonderment around three different parts. Are there currently rules governing employer-sponsored plans that make it difficult for employers to allow part-time employees to participate? Is it costly for employers to include part-time workers? Is it a combination of these, or are there yet other concerns that I have not considered? Any one or all of you.

Dr. MUNNELL. I think that Jamie is probably the expert here, but my understanding is that ERISA allows companies not to include part-time employees, and so there is a temptation not to do that.

I think that if you were going to just do part-time employees generally, there would be a lot of coming and going that would make it expensive. But when you add this requirement, that it is the long-term part-time employee, 3 years or so, I think that is a very sensible criterion for including that kind of person in the plan.

Mr. KALAMARIDES. Long-term part-time employees can be excluded from 401(k) plans, and there are a number of reasons, from a cost perspective, that businesses do not include them.

By expanding the definition to allow them to participate and allowing those workers to be included, you can dramatically increase access to workplace-based retirement plans.

It is important, also, to couple this with passing reforms to open multiple-employer plans to allow those long-term part-time employees at small businesses without access to be able to save there.

By doing that, long-term part-time employees who might move from employer to employer can reduce the portability challenges, because they might be in one geographic area and participate in one multiple-employer plan.

Senator GRASSLEY. My last question I will submit for answer in writing. Thank you.

Senator SCOTT. Thank you, Senator Grassley.

I would like to thank my colleagues, the witnesses, and all of the staff who have worked very hard to prepare for this hearing.

We have had a good discussion here today. My hope is that we continue these discussions offline and keep working toward enacting legislative proposals that can benefit as many Americans as possible to plan and prepare for retirement.

I look forward to working with my colleagues on this effort and hope that they will continue to reach out to the chairman with any ideas they might have in this regard.

As for today's hearing, if any member wishes to submit written questions for the record, please get them to us by the close of business on Friday, February 12th.

Thank you. With that, this hearing is adjourned.

[Whereupon, at 11 a.m., the hearing was concluded.]

APPENDIX

Additional Material Submitted for the Record

Prepared Statement of Thomas A. Barthold, Chief of Staff, Joint Committee on Taxation [1]

My name is Thomas A. Barthold. I am Chief of Staff of the Joint Committee on Taxation. It is my pleasure to present the testimony of the staff of the Joint Committee on Taxation today concerning retirement saving.

Tax subsidies for retirement savings are designed to encourage employers to offer retirement plans to their employees and to encourage individuals to contribute to plans available in the workplace, as well as to IRAs. These subsidies have led to the widespread availability of employer-sponsored retirement plans and to the accumulation of significant amounts in those plans and in IRAs.

Nonetheless, concern about the adequacy of savings to provide income security during retirement is a frequent topic of public discussion and of congressional attention. Costs associated with sponsoring a retirement plan may discourage some employers, particularly small employers, from establishing a plan. In addition, even employees with access to a workplace plan may not take full advantage of it, and savings intended for retirement may be used for other purposes (referred to as "leakage") and not replaced.

The Joint Committee staff has prepared a detailed review [2] of—

- Present law related to employer-sponsored tax-favored retirement plans and individual retirement arrangements;
- Economic issues relating to retirement plans;
- Data relating to retirement savings; and
- Summaries of selected legislative proposals relating to tax-favored retirement savings.

In connection with the work last year of the bipartisan Finance Committee Tax Working Groups, the report issued by the Savings and Investment Working Group focused on the area of private retirement savings and identified three key goals for policy makers: (1) increasing access to tax-deferred retirement savings; (2) increasing participation and levels of savings; and (3) discouraging leakage while promoting lifetime income.[3]

In the slides that follow I review those goals identified by the Working Group report and review various legislative proposals relating to each of those goals.

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[1] This document may be cited as follows: Joint Committee on Taxation, "Testimony of the Staff of the Joint Committee on Taxation Before the Senate Committee on Finance Hearing on Helping Americans Prepare for Retirement: Increasing Access, Participation, and Coverage in Retirement Savings Plans" (JCX–4–16), January 28, 2016. This document can also be found on the Joint Committee on Taxation website at *www.jct.gov*.

[2] Joint Committee on Taxation, "Present Law and Background Relating to Tax-Favored Retirement Saving and Certain Related Legislative Proposals" (JCX–3–16), January 26, 2016.

[3] The Working Group report is available at *http://www.finance.senate.gov/imo/media/doc/The%20Savings%20&%20Investment%20Bipartisan%20Tax%20Working%20Group%20Report.pdf*.

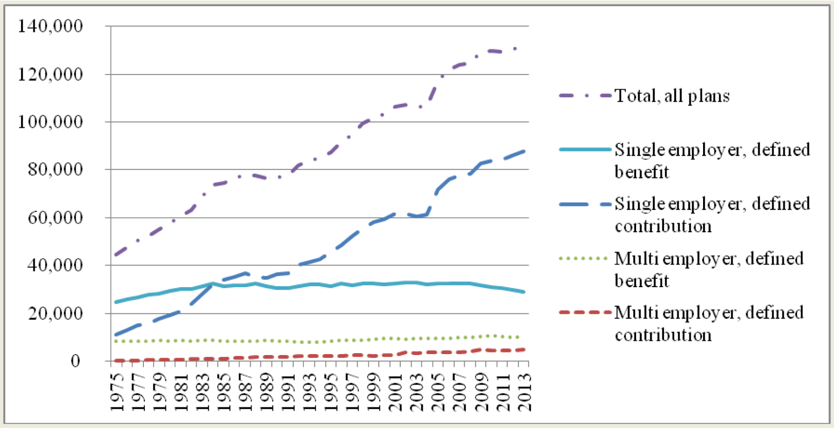
Employer-Sponsored
Tax-Favored Defined Contribution Plans

- ❑ Defined Contribution Plans
  - ❖ Benefits based on individual accounts for employees, consisting of employer and employee contributions and earnings
  - ❖ Employee benefits from investment gain and bears risk of investment loss
- ❑ Types of Defined Contribution Plans
  - ❖ Qualified retirement plans, including section 401(k) plans
  - ❖ Section 403(b) plans for charities and public schools
  - ❖ Section 457(b) plans for State and local governments
- ❑ Types of contributions to defined contribution plans
  - ❖ Employee elective deferrals
    - ■ Employee elects plan contribution in lieu of taxable current pay
    - ■ "Automatic enrollment"—deferrals begin automatically at a specified default rate unless the employee elects out or elects a different rate
    - ■ Employee deferrals may be pretax ("traditional") or after-tax Roth
  - ❖ Matching employer contributions
    - ■ Contribution must be conditioned on employee making an elective deferral (traditional or Roth) or can be conditioned on after-tax employee contributions
  - ❖ Nonelective employer contributions
    - ■ Employer decides the amount of the contribution, not based on employee contribution
  - ❖ After-tax employee contributions—generally elective, not a common plan feature

Individual Retirement Arrangements
(IRAs)

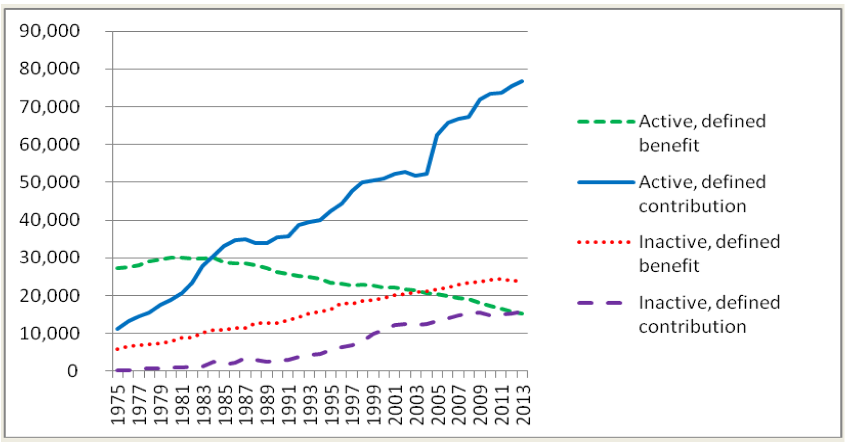
- ❑ Individual savings vehicles rather than employer-sponsored
- ❑ Account-based arrangements, like defined contribution plans
- ❑ Individual benefits from investment gain and bears risk of investment loss
- ❑ Some employer-sponsored plans funded using IRAs
  - ❖ Simplified employee pension ("SEP") plan
  - ❖ SIMPLE IRA plan

Private Sector Plan Participants by Type of Plan 1975–2013 (thousands)



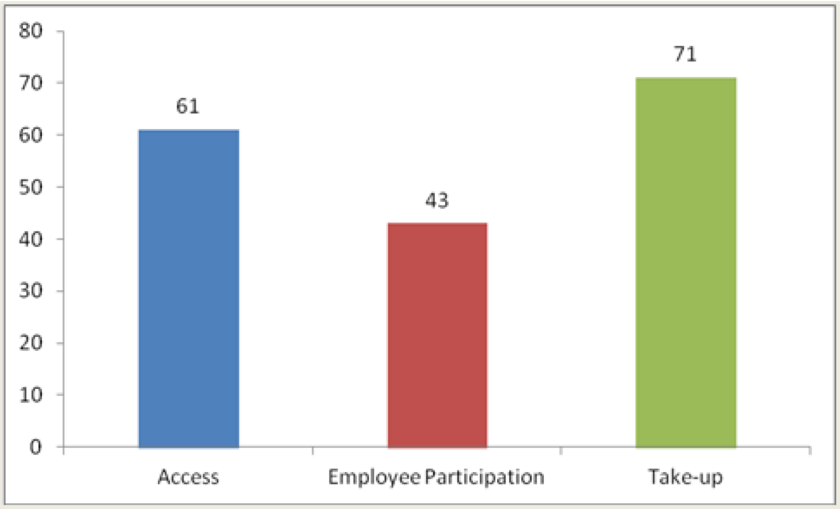
Source: Form 5500 filings with the U.S. Department of Labor.
Note: The term "Participants" refers to active, retired, and separated vested participants not yet in pay status. The number of participants also includes double counting of workers in more than one plan. For Form 5500 Short Form filers, this number may also include deceased participants whose beneficiaries are receiving or are entitled to receive benefits. Excludes plans covering only one participant.

Private Sector Plan Participants by Active or Inactive Status and Type of Plan 1975–2013 (thousands)



Source: Form 5500 Filings with the U.S. Department of Labor.

Access, Employee Participation, and Take-up Rates for Defined Contribution Plans in the Private Sector
(percentage)



Source: Bureau of Labor Statistics, National Compensation Survey Data, 2015.
Note: All workers=100 percent

Impediments to Retirement Saving

- ❑ Lack of access to workplace plans; costs associated with sponsoring a retirement plan may discourage some employers, particularly small employers, from establishing a plan
- ❑ Plan may cover only some employees and low participation rates (no contributions or insufficient contributions) by employees who are covered
- ❑ Use of savings before retirement without replacement by rollovers or additional contributions ("leakage") and lack of "lifetime income" options

Tax-Favored Retirement Savings—Key Policy Goals*

- ❑ Increasing access to retirement plans
- ❑ Increasing participation and contribution levels
- ❑ Discouraging leakage and promoting lifetime income

*These policy goals and the legislative proposals herein were discussed in the report issued in July 2015 by the bipartisan Finance Committee Tax Working Group on Savings and Investment, available at *http://www.finance.senate.gov/imo/media/doc/The%20Savings%20&%20Investment%20Bipartisan%20Tax%20Working%20Group%20Report.pdf.*

Increasing Access to Plans: Multiple-Employer Plans

- ❑ Present-law multiple-employer plans
  - ❖ A multiple-employer plan is a single plan maintained for employees of unrelated employers; offers opportunity for centralized administration and lower costs
  - ❖ Common interest requirement
    - ■ DOL indicates participating employers must share some connection (sometimes referred to as a common interest). Otherwise, the arrangement is treated as a collection of plans, each covering the employees of a particular employer
    - ■ The common interests are "genuine economic or representational interests unrelated to the provision of benefits . . ."
  - ❖ Violation with respect to one employer ("one bad apple")
    - ■ A violation of Code requirements with respect to one employer (such as failure to cover a nondiscriminatory group of that employer's employees) may cause disqualification of entire plan
    - ■ ERISA violation with respect to part of plan could create ERISA liability for all employers
- ❑ Proposals on multiple-employer (or "pooled employer") plans—S. 1270, sec. 207; S. 1970, secs. 2–3; S. 1979, secs. 201–202
  - ❖ No common interest among participating employers required; limited to defined contribution plans
  - ❖ "Designated plan provider" (S. 1270) or "pooled plan provider" (S. 1979)
    - ■ Professional service provider designated under the terms of the plan to perform all administrative duties reasonably necessary to ensure that plan meets qualification requirements and each participating employer meets its responsibilities
    - ■ Provider required to register with IRS or DOL and subject to credentialing/oversight
    - ■ May have fiduciary liability to the extent not delegated under the proposal to a participating employer
  - ❖ Solution for "one bad apple"
    - ■ Each employer bears fiduciary responsibility for the selection and monitoring of the pooled plan provider and for the investment of assets attributable to the employer's employees if not delegated to another fiduciary, but not for plan assets as a whole
    - ■ The failure of a Code requirement with respect to the portion of the plan covering employees of a particular employer causes disqualification of only that portion of the plan, which may be spun off from the plan

Increasing Access to Plans: Start-up Costs

- ❑ Present-law credit for small employer pension plan start-up costs
  - ❖ Nonrefundable tax credit for administrative costs of a small employer for adopting/administering a new qualified retirement plan, SIMPLE IRA plan, or SEP
  - ❖ Credit limited to lesser of $500 per year or 50 percent of qualified start-up costs and only allowed for 3 years
  - ❖ Plan must cover at least one lower-paid employee
  - ❖ Small employer—no more than 100 employees

- ❖ No requirement to continue plan (or continue at same level) in post-credit period
- ❖ To date, take up for this credit has been very weak. Total value of the credit is often in the range of half a million dollars annually.

❑ Proposals to expand the present-law credit for plan start-up costs

- ❖ S. 1270, sec. 202—Retains credit as 50 percent of costs, but increases maximum credit to the greater of $500 or lesser of (1) $250 x number of nonhigh participants or (2) $5,000
- ❖ President's FY 2016 budget proposal—Qualified costs are expanded to include employer contributions and maximum credit is increased to $1,500 ($2,000 if new plan includes automatic enrollment); credit of $500 for existing plan that adds automatic enrollment

Increasing Access to Plans:

New 401(k) Automatic Enrollment Safe Harbors and Related Credit

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❑ Existing automatic enrollment safe harbor for nondiscrimination testing

- ❖ Present-law safe harbor requires default rate of not less than 3 percent but not more than 10 percent for first year, then requires escalation of minimum default rate to 4 percent, 5 percent, and 6 percent in subsequent years but not above 10 percent; 6 percent deferral needed for full required safe harbor employer match
- ❖ Related safe harbor for matching contributions limits matches to 6 percent

❑ S. 1270, sec. 220; S. 1970, sec. 4—Secure deferral arrangements

- ❖ Requires automatic enrollment with higher default percentages (minimum default rate of between 6 percent and 10 percent for first year, increasing to 8 percent and 10 percent in subsequent years, with no maximum rate); 10 percent deferral needed for full required safe harbor employer match
- ❖ Related safe harbor for matching contributions allows matches up to 10 percent (rather than 6 percent maximum under present law)

❑ Credit for small employer (up to 100 employees) maintaining a secure deferral arrangement

- ❖ S. 1270, sec. 220—Credit for 3 years of 10 percent of the matching and nonelective contributions made for nonhighs, subject to an annual credit cap of $10,000
- ❖ S. 1970, sec. 5—Credit for a nonhigh employee's first 5 years of participation for matching contributions up to 2 percent of compensation, with no annual credit cap

Increasing Participation and Contribution Levels:

Coverage for Long-Term, Part-Time Workers

❑ Present-law minimum participation rules under the Code and ERISA allow employees to be excluded until earning a "year of service," generally 1,000 hours worked in a 12-month period, and reaching age 21. A parallel rule applies under section 401(k).

❑ Proposals require a 401(k) plan to allow "long-term part-time" employees to contribute to the plan—H.R. 2117, sec. 103; President's FY 2016 Budget Proposal

- ❖ Long-term part-time defined as at least 500 hours of service annually for 3 years
- ❖ Age 21 exclusion still permitted
- ❖ Employer contributions not required, but, if made, years of service with at least 500 hours count towards vesting
- ❖ Flexibility provided on how long-term part-time employees treated in nondiscrimination testing

Increasing Participation and Contribution Levels: Present-Law Saver's Credit

- ❑ A nonrefundable tax credit for eligible taxpayers who make elective deferrals (or voluntary after-tax contributions) to tax-favored retirement plans or contributions to IRAs
- ❑ Only contributions up to $2,000 taken into account
- ❑ Tax credit limited to a specified percentage (50 percent, 20 percent, or 10 percent) of contributions, depending on taxpayer's adjusted gross income (for 2016, ranging from $37,000 to $61,500 for joint filers; $18,500 to $30,750 for single)
- ❑ Tax credit is in addition to any deduction or exclusion for contributions
- ❑ Credit is available to individuals who are 18 or older, other than full-time students or individuals claimed as a dependent on another taxpayer's return
- ❑ Credit reduced for distributions from plans or IRAs during a specified period

Increasing Participation and Contribution Levels: Expansion of Saver's Credit

- ❑ H.R. 2117, sec. 105
  - ❖ Credit is 50 percent of eligible contributions up to $500 for each eligible individual with AGI not exceeding an indexed dollar amount (initially $65,000 for joint filers ($32,500 for single) with phase-out over next $20,000 ($10,000 single))
  - ❖ Credit refundable
  - ❖ Doubled (100 percent of contributions) if taxpayer agrees to have entire credit amount contributed directly to a tax-favored retirement plan
  - ❖ $500 contribution amount increases to $1,500 by 2023, indexed thereafter
  - ❖ Treated as a pretax contribution (taxable upon distribution), but does not count against contribution limits; treated as employer contribution for nondiscrimination purposes

Discouraging Leakage and Promoting Lifetime Income

- ❑ Sources of leakage
  - ❖ Exceptions to 10 percent early distribution tax for withdrawals for special purposes
  - ❖ Hardship withdrawals for immediate need for funds
  - ❖ Plan loans and inability to repay loan balance may diminish retirement funds
    - ■ On termination of employment, plan terms may accelerate loan repayment and provide for offset of unpaid loan balance against employee's plan account (which includes loan note)
    - ■ Regular 60-day rollover period may not provide sufficient time to restore funds

Discouraging Leakage and Promoting Lifetime Income: Plan Loan Not Repaid

- ❑ S. 606, secs. 2 and 4
- ❑ Proposal extends the time for rollover of plan loan offset amount until the due date for the return for the year in which the offset occurs
  - ❖ Plan loan offset amount—Account balance offset after acceleration of loan repayment under plan terms results in actual rather than deemed distribution

- ❖ As an actual distribution, a plan loan offset amount can be an eligible rollover distribution
  - ■ Under present law, only 60-day rollover available
  - ■ Participant may not know loan offset date or be able to find money within 60 days to rollover

❑ No debit/credit card-type loans from plans

- ❖ Prevents participant from using plan loans for daily regular purchases and the risk of incurring revolving debt that may not be fully repaid

Discouraging Leakage and Promoting Lifetime Income: Hardship Distributions

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❑ S. 606, sec. 3; S. 1270, sec. 214

❑ No suspension of deferrals after hardship withdrawal

- ■ Present law requires a 6-month suspension of new elective deferrals following a hardship distribution

Discouraging Leakage and Promoting Lifetime Income: Portability of Lifetime Income Investment

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❑ Lifetime Income

- ❖ Concept—benefits withdrawn in a form that provides payments for entire lifetime, regardless of longevity; includes annuities and other forms, such as structured installment payments
- ❖ Defined benefit plans—must offer annuity benefits
- ❖ Defined contribution plans and IRAs—annuity and other lifetime income options not common; when offered, a lifetime income product may be an investment option under the plan or lifetime income may be a distribution option when benefits commence

❑ In order to preserve retirement savings for retirement, present law limits plan distributions before termination of employment ("in-service" distributions)

❑ If a lifetime income product is discontinued as an investment option under a plan, restrictions on in-service distributions may prevent transfer of the investment to another plan or IRA.

❑ Participant may be required to liquidate investment and reinvest in different option, losing benefit of lifetime income feature.

❑ S.1270, sec. 221; President's FY 2016 Budget

- ❖ Allows in-service transfer to another retirement plan or IRA of lifetime income investment when investment options under a plan are changed

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QUESTIONS SUBMITTED FOR THE RECORD TO THOMAS A. BARTHOLD

QUESTION SUBMITTED BY HON. ORRIN G. HATCH

Question. Mr. Barthold, you mentioned part-time workers in your testimony. The working group identified proposals that would target "long-term" part time workers, so-called "career part-time" workers who spend 3 or more years in part-time status working for the same employer. As more workers spend lengthy portions of their careers in part-time employment, this seems like an issue that needs to be explored. What are the obstacles to such coverage today, and are they primarily legal or economic in nature?

Answer. For 2015, the percentage of part-time workers participating in a retirement plan is less than one-third of the percentage for full-time workers, 19 percent

versus 59 percent.[1] This difference in participation is partially explained by a lack of access. The percentage of part-time workers with access is close to one-half the percentage of full-time employees with access (37 percent versus 76 percent). The difference in the rate of participation is also explained by the relatively low take-up rates of part-time employees who are offered access: 51 percent of part-time employees with access choose to participate in a retirement plan versus 78 percent for full-time workers. This lower take-up rate may reflect a rational choice by part-time employees to value current cash compensation over deferred compensation under a retirement plan. Part-time employees tend to be lower income. These employees may require a greater portion of their current earnings to obtain basic necessities, leaving a smaller portion available for other purposes, which include retirement savings.

This reduced take-up rate may, in turn, partly explain the lower access rate. The requirements under Internal Code Revenue ("Code") and the Employee Retirement Income Security Act of 1974 for retirement plans allow employers to exclude employees who have not completed 1,000 hours of service in a year.[2] When take-up rates are low, employers may conclude that part-time employees place a lower value on access to retirement benefits than do full-time employees or than part-time employees place on other forms of compensation, and thus may decide not to cover them.

Other factors may also influence an employer's decision on whether to cover part-time employees under its retirement plan. Offering coverage to part-time workers may result in greater administrative costs to employers, such as costs associated with additional employee notices and record keeping costs associated with small account balances.[3]

QUESTIONS SUBMITTED BY HON. DEAN HELLER

Question. What is the most important thing lawmakers can do right now to help small businesses offer a workplace savings plan to their employees?

Answer. As explained below, a combination of measures, such as those considered by the Senate Finance Committee's Savings and Investment Working Group, may be needed to help small businesses offer retirement plans to their employees.

According to economic theory, the amount and forms of compensation provided by an employer to its workforce are based on its business assessment of the compensation needed to hire and retain the workforce necessary for the firm's success. One basic factor in an employer's decision whether to offer a retirement plan is the perceived value of the plan to the employees.

Plan contributions (whether made at the election of the employee or employer matching or nonelective contributions), and the administrative costs associated with a retirement plan, form a part of employees' compensation. The value of the plan to employees therefore depends on their preference for compensation in the form of retirement plan contributions, rather than other forms, particularly current wages. Depending on a particular employee's circumstances, competing uses for current wages (rather than retirement plan contributions) may consist of basic living expenses (for example, for very low-earning employees), paying off debt (for example, student loans, mortgage, credit cards), and saving for other, generally nearer-term purposes (for example, emergencies, buying a home, children's education). If employees place a lower value on the retirement plan than it costs the employer to provide the plan, the employer may not retain the employee's services or the employer may not provide the retirement benefit.

Employers may have an incentive to offer a retirement plan if the cost is subsidized by the government. This would make it more likely the value the employee

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[1] *See* Figure 4 on page 58 in Joint Committee on Taxation, "Present Law and Background Relating to Tax-Favored Retirement Saving and Certain Related Legislative Proposals" (JCX–3–16), January 26, 2016, which provides a chart comparing access, participation, and take-up rates between full-time and part-time employees in qualified retirement plans for 2015.

[2] These rules are explained in more detail in JCX–3–16 at page 11.

[3] Rules prohibiting qualified retirement plans from discriminating in favor of highly compensated employees (as defined in the code) allow employees who have not completed 1,000 hours of service in a year (and employees under age 21 who may also be excluded) to be tested separately for nondiscrimination. However, for an employer that allows participation by these employees, this separate testing results in some additional administrative cost. The nondiscrimination requirements are described in more detail in JCX–3–16, pages 12 to 15.

places on the retirement benefit exceeds the employer's cost of providing the benefit. For example, a tax subsidy of 25 percent on the costs of the plan means an employer can offer its employees $1 of compensation at $0.75 cost. This is attractive to the employer, even if the employee values the $1 of compensation at exactly $1 and no more.

The reasons why not all employers offer plans—as well as why not all employees who are offered plans choose to participate—therefore depend on the characteristics of a particular employer and its employees. As a result, effective incentives to expand retirement plan access and participation are likely to vary across employers and their employees, so a combination of legislative changes may be needed.

Question. As you know, current law provides a tax credit of up to $500 per year, for 3 years, for start-up costs related to qualified small employer plans. However, the uptake rate for this credit has been historically weak. Why do you think the uptake has been so low?

Answer. As noted above, the administrative costs associated with a plan, as well as plan contributions, form part of employees' compensation. As previously suggested, a likely reason for an employer not to offer a plan is an assessment that employees prefer to receive compensation in other forms. By reducing the administrative cost of a plan, the start-up credit frees up funds to be provided to employees in other, preferred forms of compensation. However, the reduction in cost may not be sufficient to change the value of the plan to employees, as the "cost" to the employees is the difference in value they place on retirement plan benefits compared to their preferred form of compensation (or how much less they value increased future consumption at the expense of current consumption). In addition, because the start-up credit is part of the general business credit, an employer that is eligible for other credits may not be able to benefit from the start-up credit for the taxable year in which the plan costs are incurred.

Question. If we were to expand the start-up credit, as other legislative proposals have suggested, including the President, what is the fiscal impact?

Answer. An expansion of the tax credit results in a revenue loss. In the case of the start-up credit, the potential loss consists of both employer income taxes due to the credit and employee income taxes (and, generally, payroll taxes) as part of employees' compensation shifts from taxable wages to excludable retirement plan benefits. The fiscal impact of a particular proposal will depend on the details of the proposal. Moreover, the more effective incentive a particular proposal provides for employers to offer plans, the greater the revenue loss as more currently taxable employee wages shift to retirement plan contributions.

Question. I am deeply concerned with leakage. In my home state, we have felt the pressures of the recession and many of the constituents have had to dip into their retirement funds to make ends meet. In your opinion, what is the single best way we as lawmakers can make it easier for workers to return assets for retirement accounts after they have been withdrawn?

Answer. There is no single best solution for retirement plan leakage. One challenge for increasing retirement savings for lower- and middle-income workers is that these workers may be reluctant to save for retirement if there is no opportunity to access these funds for purposes other than retirement, such as in the event of financial hardship or for other nonrecurring unexpected expenses. Elements of the current statutory structure reflect these competing aspects of retirement savings by imposing an additional income tax on withdrawals of retirement savings before age 59½ but including a number of exceptions for withdrawals for particular purposes. Further, present law provides rules that limit withdrawals of elective retirement savings from 401(k) plans during employment but allow withdrawal in the event of financial hardship. However, to the extent that an individual views retirement savings as an available resource for other needs, the savings become general savings rather than retirement savings, serving an important need for individuals, but not entirely fulfilling the purpose for which the tax subsidy is provided. Once these amounts are withdrawn and consumed, it is often very difficult for these workers to replace (or return) this withdrawn retirement savings. Further, returning withdrawn savings may be particularly difficult to combine with continuing the same prior level of ongoing retirement saving. On the other hand, reducing opportunities for workers to access retirement funds for other critical uses may also result in decreased retirement savings as individuals opt for more accessible means of savings. Thus, allowing some access to retirement savings may increase aggregate retire-

ment savings even though, in a number of individual cases, retirement savings may decline.

In addition to a concern that individuals may simply be unable to return withdrawn amounts, allowing individuals to withdraw from retirement savings and return these withdrawn funds creates a number of compliance issues (as well as complexity and recordkeeping issues) for both the individual and the Internal Revenue Service. These issues are particularly problematic when the withdrawal and the return of assets occur in different tax years. Recognizing these issues, present law limits the situations to 60-day rollovers for actual withdrawals and return of funds, with the opportunity for extension in limited circumstances.

Plan loans through employer-sponsored retirement plans are one means by which plan participants can gain access to plan funds for nonretirement purposes and then repay the funds over time, generally through payroll deduction. The Code allows this without income tax inclusion of the loaned amount if certain requirements are satisfied. These include charging a market rate of interest on the loan and that the loan generally be repaid in equal amortized installments over 5 years.

One maxim that may be particularly appropriate in this area is to be careful to avoid unintended consequences. For example, any proposal intended to make it easier for individuals to access retirement savings for other uses and return the funds tax-free may have the result of encouraging such withdrawals that individuals cannot realistically return, resulting in decreased rather than increased retirement savings. On the other hand, reducing opportunities for workers to access employer-sponsored retirement funds for other critical uses may also result in decreased employer-sponsored retirement savings as workers opt for more accessible means of savings. However, it is important to note that savings for retirement may take forms outside employer-sponsored plans or even IRAs. Any individual asset accumulation before retirement is potentially available for retirement.

Question. I strongly believe that tax reform, done the right way, can improve our fiscal picture. What steps can we as lawmakers take to improve our retirement savings in a fiscally responsible way?

Answer. Any changes in tax law, including tax reform, involve balancing competing goals and interests. As discussed above in connection with the start-up credit, the more effective incentive a particular proposal provides employers to offer plans and employees to contribute, the greater the revenue loss associated with the proposal. It may be appropriate to consider offsetting the effects of expanded retirement savings with other reforms, either in the retirement savings area or in other parts of the tax system.

Question. I understand the President is expected to propose an Open MEP plan in his FY17 budget. I would imagine a significant amount of implementing guidance would be needed. If Open MEPs were expanded, what role, if any, would the IRS play in this additional guidance?

Answer. An open multiple-employer plan, or Open MEP, is a single plan maintained by unrelated employers. A proposal relating to Open MEPs is contained in *General Explanations of the Administration's Fiscal Year 2017 Revenue Proposals,* pages 147–149, Department of the Treasury, February 2016, available at *https://www.treasury.gov/resource-center/tax-policy/Documents/General-Explanations-FY2017.pdf.* In addition to changes under the Employee Retirement Income Security Act of 1974 ("ERISA"), the proposal involves responsibilities both for the service provider promoting and administering an Open MEP, and for participating employers, with respect to establishing and maintaining the tax-favored status of the plan. The proposal refers to guidance to be issued by the Secretary of the Treasury; however, as a practical matter, guidance with respect to code provisions is developed and issued by the IRS, subject to Treasury review and approval. In addition, the Open MEP proposal provides for guidance by the Department of Labor and requires Treasury and Labor guidance to be coordinated and consistent.

Question. Like many Nevadans, I am a strong supporter of ways to help our vulnerable populations save long-term for our retirement. What is the single most important thing lawmakers can do right now to help low-income and moderate-income families prepare for retirement?

Answer. As discussed above, in light of the variety of circumstances among employers and employees, a combination of measures is likely to be needed, rather than any single measure.

QUESTION SUBMITTED BY ROBERT P. CASEY, JR.

Question. In your opinion, what are the most efficient policy options available to make it easier for businesses to help their employees save, or individuals save on their own, and for whom will that most improve retirement and savings outcomes?

Answer. As discussed in other responses, an employer provides employees with the amount and forms of compensation that it determines are needed to hire and retain the workforce necessary for the firm's success. Plan contributions, and the administrative costs associated with a retirement plan, form a part of employees' compensation. Thus, a basic factor in an employer's decision whether to offer a retirement plan is the perceived value of the plan to the employees.

The value of the plan to employees depends in turn on their preference for compensation in the form of retirement plan contributions, rather than other forms, particularly current wages. Depending on a particular employee's circumstances, competing uses for current wages (rather than retirement plan contributions) may consist of basic living expenses (for example, for very low-earning employees), paying off debt (for example, student loans, mortgage, credit cards), and saving for other, generally nearer-term purposes (for example, emergencies, buying a home, children's education).

Individuals also have the option of saving for retirement by contributing to IRAs. This again involves an individual's decision to favor retirement saving over competing uses for the same funds, such as basic living expenses, paying off debt, or saving for other purposes, as described above.

Employers may have an incentive to offer a retirement plan if the cost is subsidized by the government. This would make it more likely the value employees place on the retirement benefit exceeds the employer's cost of providing the benefit. For example, a tax subsidy of 25 percent on the costs of the plan means an employer can offer its employees $1 of compensation at $0.75 cost. This is attractive to the employer, even if the employee values the $1 of compensation at exactly $1 and no more.

Tax incentives may therefore play a role in encouraging employers to offer retirement plans and in encouraging individuals to save for retirement. However, the reasons why not all employers offer plans, as well as why not all individuals choose to contribute, depend on the particular characteristics of an employer and of each individual. As a result, a combination of policy options may be warranted to make it easier for businesses to help their employees save or individuals save on their own.

PREPARED STATEMENT OF HON. MICHAEL B. ENZI,
A U.S. SENATOR FROM WYOMING

Mr. Chairman, I would like to thank you for organizing this hearing and for your consistent support of retirement plan options, specifically Multiple Employer Plans. I would also like to thank the expert witnesses here today who will speak further as to how we can make it easier for small businesses to provide retirement benefits for their employees. I would like to extend a special welcome to Mr. Kalamarides, who has been willing to testify at now three Senate hearings on this topic, including a hearing I held in the HELP Retirement Security Subcommittee in October.

A critical challenge in enhancing the retirement security for all Americans is expanding plan coverage among small businesses. To address this, I believe we need to make retirement plans less complicated, intimidating, and expensive for small businesses. One way to do this is by allowing the expansion of Multiple Employer Plans.

Multiple Employer Plans (MEPs), which have been permitted under ERISA and Federal tax law for decades, allow small businesses to join together to make retirement plans much easier to manage and significantly less expensive to provide for owners of those businesses, all while maintaining the highest levels of quality. Under current law, Multiple Employer Plans must consist only of employees that are joined together by significant interests unrelated to the provision of benefits. It seems to me that access to Multiple Employer Plans can and should be broadened to provide small businesses with administrative simplicity with regard to retirement benefits.

This past year, the bipartisan Senate Finance Committee Savings and Investment report included a recommendation to allow employers to join together to open Multiple Employer Plans. The report notes, however, that current law "hinders the formation of Multiple Employer Plans." I believe this committee has a great opportunity to remedy those hindrances.

My interest in MEPs is based on my experience as a former small business owner and view that Congress can help narrow the retirement coverage gap in America. I believe we can do this by helping the expansion of plan options for small businesses, including Multiple Employer Plans, specifically by allowing the broadening of diversity among those businesses within such plans.

We have a retirement coverage gap in America. I think one of the best ways to close that gap is to make it easier for small businesses to enter into a MEP by relaxing regulations and creating a more flexible environment. I commend the chairman and many of my colleagues on this committee for their work to advance legislation that fixes many of the issues preventing businesses from entering into such plans. I look forward to working in a bipartisan way to finalize legislation that will, once and for all, ensure that small businesses have the flexibility necessary to help close the retirement gap.

PREPARED STATEMENT OF HON. CHUCK GRASSLEY, A U.S. SENATOR FROM IOWA

Mr. Chairman, I would like to start by thanking you for holding this important hearing focused on enhancing retirement savings options. This committee has made great strides over the years in enacting bi-partisan policies aimed at encouraging individuals to save and employers to offer retirement plans.

I am proud to have been part of enacting some of the most sweeping retirement savings reforms in the past decade as part of the Pension Protection Act of 2006. These reforms included increasing contribution limits, encouraging greater participation in retirement savings through auto enrollment, making permanent the savers credit and allowing for catch-up contributions. It also made permanent a tax credit to help small businesses with plan start-up costs. These reforms were all good steps, but there is always room for improvement.

The Savings and Investment tax reform working group did a good job of identifying several areas where there is bipartisan overlap. One proposal that appears promising is removing barriers that stand in the way of small businesses joining together to offer retirement plans through a multiple employer plan.

I look forward to working with my colleagues on this committee to improve and expand upon current retirement savings options.

PREPARED STATEMENT OF HON. ORRIN G. HATCH, A U.S. SENATOR FROM UTAH

WASHINGTON—Senate Finance Committee Chairman Orrin Hatch (R–Utah) today delivered the following opening statement at a hearing examining ways to empower job creators to offer and increase access to retirement savings plans for their employees:

I'd like to welcome everyone to this morning's hearing on the ongoing effort to increase access, participation, and coverage in retirement savings plans.

Financial security, and retirement policy in particular, have never been more important. Today we will discuss policies designed to incentivize employers to set up retirement plans and to help employees save more for their retirement and make those savings last a lifetime.

When we talk about the status quo of retirement policy, there is both good news and bad news.

The good news is that the private employer-based retirement savings system—particularly 401(k) plans and Individual Retirement Accounts, or IRAs—has become the greatest wealth creator for the middle class in history.

Under the current system, millions of Americans have managed to save trillions of dollars for retirement. In specific terms, thanks in large part to policies Congress has enacted over the years, American workers have saved more than $4.7 trillion

in 401(k) plans and more than $7.6 trillion in IRAs. That's more than $12 trillion in total, more than double the amount workers had saved in 2000, despite the Great Recession, the market downturn in 2008, and historically low interest rates since that time.

Once again, that's the good news.

The bad news is that, with the retirement of the Baby Boom generation, the fiscal pressure on public programs designed to benefit retirees—programs like Social Security and Medicare—is growing exponentially, putting enormous strain on the Federal budget and driving the expansion of our long-term debt and deficits. As this pressure mounts, participation in private retirement plans will be more and more important.

Yet, at the same time, as part of the constant drumbeat here on Capitol Hill for more revenue to pay for increased spending, some have proposed reducing the allowed contributions to 401(k) plans and IRAs. That, in my view, would be both short-sighted and counterproductive.

Over the years we've learned that, for most American workers, successful retirement saving largely depends on participation in a retirement plan at work. Unfortunately, many employers, mostly small businesses, don't sponsor plans for their employees.

There are a number of reasons why an employer might opt to not offer a retirement plan, including cost, complexity, or administrative hassle. But, whatever the reason, the result is the same: fewer American workers are likely to save for retirement than would otherwise be the case.

As everyone will recall, last year, the committee established bipartisan Tax Reform Working Groups to examine all major areas of U.S. tax policy and identify opportunities for reform. One of those working groups focused specifically on tax policies relating to savings and investment. Today, the full committee will hear more about the various legislative proposals the Savings and Investment Working Group looked at as they considered options and produced their report.

I want to thank the two chairs of this particular Working Group—Senator Crapo and Senator Brown—for their efforts and their leadership on these issues. They looked extensively at a number of more recent proposals and, like all of our working groups, they produced an excellent report. I look forward to delving more deeply into these issues here today.

Simply put, we need to do more to encourage employers who don't sponsor retirement plans to set them up. Toward that end, one the first proposals described in the working group report would allow unrelated small employers to pool their assets in a single 401(k) plan to achieve better investment outcomes, lower costs, and easier administration. This proposal for a multiple employer plan, what some have called the "Open MEP," already enjoys bipartisan support here in Congress.

Many of our colleagues have worked hard to develop and advance Open MEP proposals, and, while I run the risk of missing some of my colleagues, I want to acknowledge the efforts of Ranking Member Wyden and Senator Brown, plus Senator Nelson, who has worked on this issue with Senator Collins on the Aging Committee, Senator Scott, and Senator Enzi, who held hearings on the Open MEP idea in the HELP Committee. And, as if that wasn't enough, just this week the Obama administration announced its support for the Open MEP idea.

Clearly, there is a lot of momentum for this proposal, which, in my view, is a good thing. Indeed, this is an idea whose time has come.

While it is important to pursue policies to encourage greater retirement savings and investment, we must also provide workers with tools to ensure that their savings do not run out before the end of their lives. That's why I have put forward proposals to encourage individuals to purchase annuity contracts to provide secure, lifelong retirement income.

Today there are obstacles in the law that discourage employers from adding annuity purchase options to their 401(k) plans and employees from purchasing annuities. We should do all we can to remove those obstacles, particularly given the decline of defined benefit pension plans in recent years.

Retirement policy has always been an especially important topic here on the Finance Committee, and it has always been bipartisan. Indeed, most of the retirement

legislation that Congress has passed in recent decades has been named for Senators from the Finance Committee—usually one from each party.

I hope this will continue even during this election year when attacks and accusations relating to retirement security unfortunately tend to gain a lot of traction. I plan to do my part to ensure that the committee focuses on advancing policies that unite both parties. If we can do that, I think we can make progress.

Before I conclude, I want to acknowledge that there is some interest on the committee in discussing the challenges facing multi-employer defined-benefit pension plans and their beneficiaries. These are important topics that affect employers, workers, unions, plan managers, the Pension Benefit Guaranty Corporation and, of course, current retirees who may be facing hardships. They also highlight the challenge of delivering on the promise of lifetime retirement income and the stakes for retirees if the system fails.

We certainly need to have a robust discussion of these matters in the committee and I plan to convene a hearing on multi-employer plans in the next work period. Today, however, I'm hoping we can focus on bipartisan proposals to increase access to retirement savings plans.

Prepared Statement of John J. Kalamarides, Head of Institutional Investment Solutions, Prudential Financial

INTRODUCTION

Thank you, Chairman Hatch and Ranking Member Wyden and members of the committee, for the opportunity to participate in today's discussion of helping Americans prepare for a secure retirement.

I am Jamie Kalamarides, Head of Institutional Investment Solutions, Prudential Retirement. Prudential is the second largest life insurer and a top ten global asset manager with over $1.1 trillion in assets under management. Prudential provides workplace based retirement solutions to all sizes of corporations, governments, unions and consumer groups.

While the current workplace-based retirement system has worked well for many, we at Prudential—like members of this committee—recognize that more can and should be done to enhance retirement savings opportunities for working Americans. We know that:

- Far too many working Americans do not have access to retirement savings programs in their workplace;
- Far too many working Americans are not participating in their plan or saving enough for a secure retirement; and
- Far too many working Americans do not have access to guaranteed lifetime income solutions through their retirement plans—solutions that relieve retirees from the challenges attendant to managing both investment and longevity risks throughout their retirement years.

We believe that the policy proposals identified by this committee's Savings and Investment Working Group, in their July 7, 2015 report, represent bipartisan opportunities to address these problems. Using the Working Group's Report as a guide, my testimony today will focus on expanding retirement coverage through the use of "open" multiple employer plans, enhancing retirement savings through an expanded saver's credit, and expanding access to guaranteed lifetime income solutions.

EXPANDING RETIREMENT COVERAGE

Open Multiple Employer Plans [1]

Prudential has long been concerned about what is often referred to as the "retirement coverage gap," that is, the absence of workplace based retirement savings op-

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[1] For purposes of this testimony, references to Open MEPs and MEPs are not intended to encompass those multiple employer plans that are sponsored by bona fide employer organizations, long permitted under the U.S. Department of Labor's interpretations. Our focus is on MEPs that have not been, but should be, permitted and encouraged in the absence of a commonality of participating employer interests.

portunities for employees in many of today's small businesses. It is well established that employer-sponsored retirement savings plans have become a critical component of the private retirement system in the U.S., and a proven tool for helping working Americans prepare for life after work. According to calculations by the nonprofit Employee Benefit Research Institute, workers earning between $30,000 and $50,000 per year are 16.4 times more likely to save for retirement if they have access to a workplace plan.

Unfortunately, tens of millions of working Americans don't have access to a plan on the job, leaving many ill-prepared to meet their financial needs after they stop working. With 10,000 individuals reaching retirement age each day, this is a large and growing problem. We know that a comprehensive retirement plan requires a three-legged stool—Social Security, personal savings, and pensions. While Social Security is a critical program, for median income earners, it replaces only 47 percent of pre-retirement income, leaving those without a workplace retirement plan with a potentially significant income gap in retirement.

The workplace retirement system works very well for employees of medium and large companies. Employees of small companies, however, are far less likely to have access to savings opportunities. According to data from the Bureau of Labor Statistics, only 50 percent of workers in firms with fewer than 100 employees have access to retirement plans at work. This compares to 89 percent for workers at larger firms.

This retirement coverage gap is especially problematic given that small employers provide jobs for a large and diverse section of the American population. Small businesses in the private sector provide over 30 million jobs for women. Small businesses employ over 12 million Latino Americans, 6 million African Americans, and 4 million Asian Americans—and yet, only 50 percent of employees of small businesses have access to a workplace retirement plan.

The retirement coverage gap can and should be narrowed. While a variety of solutions are possible, there is a growing consensus among financial institutions, consumer groups and Members of Congress [2] that one of the broadest and most expedient ways to close the gap is to expand access to multiple employer plans, or MEPs, for small employers and their employees. MEPs—single plans utilized by two or more employers—have been utilized successfully for years by trade associations and professional employee organizations. Unfortunately, tax laws and regulations discourage or prevent most small employers from taking advantage of them.

Addressing the constraints on multiple employer plans has bipartisan support in both the U.S. Senate and U.S. House of Representatives, as well as support from the U.S. Chamber of Commerce, AARP, many affinity groups, and the financial services industry. In this regard, we would also like to acknowledge the leadership role Chairman Hatch has played in recognizing the significance of expanding MEP participation and sponsorship, as well the work of the Savings and Investment Working Group, convened by the Chairman and Ranking Member.[3]

For the small employer market, multiple employer plans would enable small businesses to participate in a single, professionally administered plan that affords them economies of scale and minimal fiduciary responsibility. The plans would provide employees of those organizations the same opportunities to invest for retirement that employees of large companies already enjoy on a near universal basis via 401(k)s and similar defined contribution plans.

Small Business Retirement Survey by Prudential

In an effort to better understand why small businesses do not offer retirement plans, Prudential Retirement conducted a survey of more than 850 small employers during the months of March and April, 2015. All the survey participants were business owners who do not offer retirement plans today, and who have the responsibility for making decisions on employee benefits. Included in the survey were small businesses of between 3 and 500 employees.

[2] Legislation relating to addressing MEP issues has been introduced in the 113th Congress by Senator Hatch (S. 1270), Senators Collins and Nelson (S. 1970), and Senators Harkin and Brown (S. 1979); and in the 114th Congress by Representative Neal (H.R. 506), Senator Whitehouse (S. 245), Senators Collins, Nelson, and McCaskill (S. 266), and Representatives Buchanan and Kind (H.R. 557).

[3] The Savings and Retirement Bipartisan Work Group Report, July 2015, at page 6, indicates that "[t]o enable small employers to sponsor high quality, low cost plans, the working group recommends that the committee consider proposals that allow employers to join open multiple employer plans."

When asked un-prompted why they don't offer retirement plans for their employees, almost 50 percent cited cost as the concern. When prompted with a list of reasons, the top reasons why they do not sponsor plans include cost, administrative burden and hassle, and fiduciary concerns. Importantly 29 percent indicated a lack of understanding as to how retirement plans work.

Reflecting these concerns, baseline interest in offering a retirement plan is low. Only 14 percent of small business respondents are likely to consider offering a plan over the next 5 years. However, if provided an opportunity to offer a plan with little or no cost, most responsibility assumed by an independent trustee, and minimal retained responsibility beyond forwarding contributions, the rate of interest increases by more than 250 percent. Also, almost half indicated support for legislation that would make it easier for small businesses to provide retirement plans to their employees, with only 17 percent saying legislation is not needed.

Finally, the survey measured employers' attitudes towards offering retirement plans. Attitudes varied widely, highlighting the differing mindsets of small employers. We found that about ⅓ of employers had the most positive attitudes: That saving for retirement is very important; that programs to make it easier are very important; and, that they have a key role in the process. For the ⅓ of employers with the most positive attitudes, almost 70 percent were likely to consider offering a plan with little or no cost and minimal responsibility.

Given small businesses employ over 55 million workers, capitalizing on employer interest by offering plans which have little or no cost to employers, and minimal employer responsibility, could be an important step towards reducing the retirement coverage gap. At Prudential, we believe multiple employer plans can be part of the solution, but there are challenges—challenges to expanding MEP sponsorship and challenges to expanding MEP participation.

Challenges to Expanding MEP Sponsorship and Participation

Expanding access to multiple employer plans for small businesses and their employees will require Federal legislative and/or regulatory action. The challenges, in our view, are concentrated in four areas:

Tax Law—Section 413(c) of the Internal Revenue Code already recognizes plans maintained by more than one unrelated employer. However, it imposes a number of requirements on these plans as a condition of maintaining their tax-qualified status. As currently interpreted, some of these requirements, such as nondiscrimination rules, are applied on an employer-by-employer basis rather than a plan basis. This means that just one non-compliant employer can jeopardize the tax status of the entire plan, putting all employers at risk. This barrier is often referred to as the "one bad apple" rule.

ERISA—For purposes of ERISA, the Department of Labor treats as a single retirement plan only those multiple employer plans that are sponsored by a "cognizable, bona fide group or association of employers" acting in the interest of its members. It also requires that this group of employers have a "commonality of interest," such as operating in the same industry, and exercise either direct or indirect control over the plan. Taken together these conditions significantly limit the ability of other organizations, such as a local Chamber of Commerce, to sponsor a MEP for a diverse population of small employers.

Fiduciary Liability—Some employers—particularly small employers—shy away from offering a plan because they are concerned about the responsibilities and liabilities they might assume under ERISA as plan fiduciaries. The uptick in retirement plan litigation relating to plan fees and other factors has only exacerbated their concerns.

Enforcement—The Labor Department has expressed concern that expanding the number of "open" multiple employer plans—those sponsored by any entity other than a "bona fide group or association of employer"—could allow promoters of such plans to take advantage of small employers and their employees under the guise of offering a low cost, no liability plan.[4]

[4] Letter from Phyllis Borzi to Charles Jezeck, reprinted in "Private Sector Pensions, Federal Agencies Should Collect Data and Coordinate Oversight of Multiple Employer Plans," a GAO report to Chairman, Committee on Health, Education, Labor, and Pensions, U.S. Senate, September 2012, at page 44.

Facilitating Sponsorship of and Participation in MEPs

To make multiple employer plans more accessible to small businesses, lawmakers and regulators will need to take action on several fronts.

Tax Law

First, Treasury and IRS or Congress needs to clarify tax law so that any adverse consequences of not complying with the applicable tax qualification requirements for MEPs will be limited to the noncompliant employer, rather the entire plan and rest of its participating employers.

ERISA

Second, the Department of Labor or Congress needs to modify the ERISA requirements to allow a broader array of entities, organizations or associations to sponsor MEPs, subject to conditions that will ensure plans comply with ERISA's fiduciary requirements and minimize risk to plan sponsors and their employees. These conditions might include the following:

- The documents of the plan must identify the person(s) who will serve as the named fiduciary of the plan. That person(s) must acknowledge in writing joint and several liability for controlling and managing the operation and administration of the plan.
- The documents of the plan must identify the trustee(s) of the plan responsible for the management and control of the plan's assets and for the prudent collection of contributions to the plan.
- The documents of the plan must identify the person(s) who will act as the administrator of the plan, responsible for satisfying reporting, disclosure, and other statutory obligations.
- The plan and plan officials must maintain a fidelity bond in accordance with ERISA section 412.
- The documents of the plan must ensure that participating employers will not be subject to unreasonable restrictions, penalties, or fees upon ceasing participation in the plan.
- Inasmuch as the retirement coverage gap is most acute among smaller employers, participation in these new MEPs should be limited to those employers with no more than 500 employees. While it is likely that MEPs will appeal principally to employers with 100 or fewer employees, establishing the ceiling at 500 employees will give smaller employers ample time to grow without having to worry about identifying a new retirement savings vehicle for their employees.

Fiduciary Responsibility

Congress and regulators, in our view, should consider limiting the fiduciary responsibility of employers participating in a MEP to the prudent selection and monitoring of the MEP sponsor and the timely remittance of employee contributions. Similar to the selection of an investment manager under ERISA, such a limitation is not intended to eliminate or reduce fiduciary responsibility with respect to the management and operation of the plan, but rather appropriately allocates those responsibilities to professionals best positioned to protect the interest of plan participants and beneficiaries.

With regard to the selection and monitoring of a MEP, we believe employers, particularly smaller employers, would benefit from specific guidance addressing how they should discharge such responsibilities as an ERISA fiduciary. For example, a prudent selection process might involve an objective evaluative process that takes into account—the qualifications of the parties (fiduciary and non-fiduciary) responsible for the MEP; the scope and quality of services offered; the extent to which the MEP offers a broad range of investment options; and compliance with Federal law. With regard to monitoring responsibilities, a prudent process might involve a periodic (or annual) review of any changes in the information that served as the basis for the initial selection of the MEP.

Enforcement

The Labor Department has raised concerns about the potential for fraud and abuse should Open MEPs be permitted. We believe these concerns should be further explored in an effort to determine what, if any, additional enforcement or other authority might assist Labor in addressing such concerns.

A Safe Harbor MEP

To facilitate participation in MEPs and reduce compliance risks for small employers, the Department of the Treasury and the Internal Revenue Service, in coordination with the Department of Labor, should develop a safe-harbor model plan that minimizes the administrative complexities and costs of MEPs, is not subject to complex tax-qualification testing requirements, and enhances the ability of MEPs to generate positive retirement outcomes for plan participants.

A template we would recommend for such a model would include the following characteristics:

- A single plan, with a centrally administered trust, serving all participating employers.
- Plan participation would be limited to employers with no more than 500 employees.
- Specifically identified persons to serve as the named fiduciary, trustee(s), and administrator.
- Funded by employee contributions, with employer contributions permitted, but not required.
- Automatic enrollment of employees at a rate equal to 6 percent of pay, with employees eligible to opt out or select an alternative contribution rate.
- Automatic escalation of employee contributions to 10 percent of pay, in annual 1 percent increments, with employee opportunity to opt out.
- Hardship withdrawals in accordance with IRS rules, but no participant loans.
- A broad range of diversified investment options.
- In the absence of investment direction, contributions would be defaulted in to a preservation of principal investment option for the first 4 years and, thereafter, into a qualified default investment alternative (QDIA) in accordance with Labor Department standards.
- At least one investment or distribution option that includes a lifetime income product.

We believe that use of a model plan, similar to the above, should avoid the need for complex and costly nondiscrimination testing and, through reduced administrative costs, increase retirement savings for plan participants.

We—at Prudential—see MEPs as a “win” for both employees and employers.

MEPs will afford employees the opportunity for better retirement outcomes. A properly designed MEP will promote savings by employees through the use of automatic enrollment and automatic escalation of their contributions. MEPs may further encourage appropriate investment behavior by providing investment options selected by investment professionals, better ensuring that plan participants will be able to tailor their portfolio to their investment goals and tolerance for risk.

Unlike IRAs, MEPs offer employees the potential for an employer match and the opportunity to save for retirement at levels more appropriate for meaningful retirement savings ($18,000 per year, as compared to $5,500 per year for 2016), as well as access to institutionally priced investments. MEP participants would further benefit from having their plan’s fiduciary and administrative responsibilities discharged by plan and investment professionals, thereby enhancing the fiduciary and other protections afforded by Federal law—the Employee Retirement Income Security Act (ERISA).

Small businesses will be better positioned to compete for talent. For employers, MEPs represent an opportunity to offer employees a meaningful opportunity to save for retirement in a tax-advantaged plan, without the administrative costs and fiduciary risks attendant to maintaining a stand-alone retirement plan. Moreover, surveys consistently show that workers consider retirement savings plans a valued employee benefit. The offering of a retirement plan, therefore, can increase an employer’s ability to attract and retain a high quality workforce and, thereby, be more competitive.

While multiple employer plans may not be the only solution to closing the retirement coverage gap, we believe it is an important one and one that should be available to substantially more employers than is the case today. For a more comprehensive discussion of MEPs and our proposals, we have attached a copy of our recent white paper, *Multiple Employer Plans—Expanding Retirement Savings Opportunities,* for your consideration. (Also available through our website at: *http://research.prudential.com/documents/rp/mep_paper_final_2015.pdf*).

State Sponsored Plans for Private Sector Employers

As members of this committee are aware, an ever increasing number of States are pursuing or considering the establishment of a State sponsored plan, with respect to which private-sector employers may be required to participate to the extent they do not otherwise offer a retirement savings program for their employees. Without a Federal solution, we are concerned that these efforts may result in complexity and confusion for smaller employers whose business and employees are not defined by State boundaries. Retirement savings programs based on zip codes will not provide a complete solution to the retirement coverage gap. A Federal solution, in our view, is an imperative. MEPs offer such a solution for employers considering retirement savings options and will complement State based solutions.

As noted above, we believe that MEPs offer small employers and their employees the opportunity for more meaningful retirement savings, as compared to the IRA-based plans under consideration by many States ($18,000 per year, as compared to $5,500 per year for 2016), as well as access to institutionally priced investments and ERISA protections. We believe, if given a choice, employers will opt to participate in an ERISA-covered MEP, rather than a State sponsored IRA-based program, but Federal legislation is necessary to provide that choice. Federal legislation also is necessary to deal with the tax qualification issues that expose participating employers, covered employees and the MEP to liability as a result of the actions of one noncompliant participating employer.[5]

ENHANCING RETIREMENT PARTICIPATION AND SAVINGS

The Report of the Savings and Investment Working Group identifies a number of items that could enhance retirement savings, particularly for lower and middle income families. In particular, we note that the Working Group supports consideration of expanding the current safe harbor for automatic enrollment, under which the employer matching contribution might be raised from 6 percent of pay up to 10 percent of pay. The Working Group also encourages consideration of proposals that allow long-term, part-time employees to contribute to employer sponsored retirement plans. And, in addition to other things, the Working Group identified a saver's credit as a means by which to further encourage lower income earners to save for retirement.

Prudential agrees with the Working Group that each of the foregoing items should be considered as we explore ways to encourage retirement savings, particularly for lower and middle-income families.

GUARANTEED LIFETIME INCOME

With an estimated 10,000 Americans reaching retirement age every day, we know that very few of those individuals are being offered the opportunity to consider a guaranteed lifetime income option as part of their retirement plan. We also know that few of today's workers are able to manage investment and longevity risks in retirement on their own. As recognized by the Council of Economic Advisers' February 2, 2012 Report, *Supporting Retirement for American Families,* this is a particularly significant issue for women, who tend to have lower retirement savings rates than men, while also having longer life expectancies. Guaranteed lifetime income solutions provide a means by which all workers can enjoy both certainty and security during their retirement years.

We are particularly encouraged by and fully support two specific proposals identified by this committee's Savings and Investment Working Group.

Lifetime Income Portability

The first is a proposal, included in Chairman Hatch's *Secure Annuities for Employees (SAFE) Retirement Act,* S. 1270 (113th Congress), that would address concerns around the portability of certain in-plan annuity features. Portability issues are raised when a plan sponsor decides to modify or eliminate an investment option with a guaranteed lifetime income feature with respect to which some participants may have invested. Under the proposal, invested participants would, upon the elimination of the investment or feature, be permitted to transfer their interest to another employer sponsored retirement plan or IRA, without regard to whether a distribution would otherwise be permitted. The elimination of issues around portability

[5] We note that, while the Department of Labor recently published an interpretive bulletin (§ 2509.2015–02, 80 Fed. Reg. 71936, November 18, 2015) to facilitate State sponsorship of MEPs, that guidance does not resolve the referenced tax qualification issues presented by one noncompliant participating employer.

would be very helpful in addressing the concerns on the part of some plan sponsors regarding the inclusion of in-plan annuity products and the discharge of their fiduciary responsibilities under ERISA.

Annuity Selection Safe Harbor

The second proposal relates to the rules governing the selection of annuity providers. In this regard, the Working Group expresses its support for consideration of policies that encourage retirees to be knowledgeable about and select distributions that provide a stream of income payments over the course of their retirement. We agree with the Working Group and fully support such policies. One challenge is encouraging employers to offer guaranteed lifetime income products to their employees as part of their retirement plan. This challenge is exacerbated by the current Department of Labor rules governing the selection of annuity providers, rules that require any employer considering the inclusion of an annuity product to assess, and assume fiduciary liability for, the ability of the annuity provider to satisfy its contractual obligations. While we recognize the importance of such determinations, we believe the burden of such assessments is appropriately the role of state insurance regulators, not plan fiduciaries.

In our experience, while most plan fiduciaries are comfortable making determinations relating to the reasonableness of costs in relation to benefits and the quality of services (requirements of the current Labor Department safe harbor), few are comfortable determining the long-term financial viability of an insurer or other financial institution. For this reason, we believe the current safe harbor standard is having a chilling effect on plan sponsor considerations of guaranteed lifetime income products. In this regard, we support approaches identified by the Working Group pursuant to which plan fiduciaries would, on questions of financial viability, look to insurers to confirm they are in good standing with State licensing, financial solvency, auditing and reporting requirements; requirements established by the States to protect their citizens, including plan participants.

CONCLUSION

We thank the chairman, the ranking member and members of the committee for the opportunity to share our views. We welcome any questions and look forwarding to working with you on these issues of critical importance to today's working Americans.

PRUDENTIAL
Bring Your Challenges

Multiple Employer Plans

Expanding Retirement Savings Opportunities

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Executive Summary

Employer-sponsored retirement savings plans have become a critical component of the private retirement system in the U.S., and a proven tool for helping working Americans prepare for life after work. According to calculations by the nonprofit Employee Benefit Research Institute, people earning between $30,000 and $50,000 per year are 16.4 times more likely to save for retirement if they have access to a workplace plan.

Unfortunately, tens of millions of Americans don't have access to a plan on the job, leaving many ill-prepared to meet their financial needs after they stop working. This retirement coverage gap is most acute among employees of small companies, many of whom do not sponsor plans due to concerns about costs, complexity, and fiduciary liability.

The retirement coverage gap can and should be narrowed. While a variety of solutions are possible, there is a growing consensus in Washington that one of the broadest and most expedient ways would be to expand access to multiple employer plans, or MEPs, for small employers and their employees. MEPs—single plans uti-

lized by two or more employers—have been deployed successfully for years by trade associations and professional employee organizations. Unfortunately, tax laws and regulations discourage or prevent most small employers from taking advantage of them. Removing those constraints is endorsed not only by several Washington lawmakers on both sides of the political aisle but also by the U.S. Chamber of Commerce, AARP, many affinity groups, and the financial services industry.

For the small employer market, multiple employer plans would enable small businesses to participate in a single, professionally administered plan that affords them economies of scale and minimal fiduciary responsibility. The plans would provide employees of those organizations the same opportunities to invest for retirement that employees of large companies already enjoy on a near universal basis via 401(k)s and similar defined contribution plans.

This paper outlines the legislative and regulatory actions that would be needed to broaden access to MEPs for small employers. It also describes the features that a model MEP might incorporate, including:

- Automatic enrollment of employees and automatic escalation of employee contributions.
- Automatic deferral of employee contributions into an investment option designed to preserve principal. After 4 years, contributions would be made to a qualified default investment alternative, such as a target-date fund.
- A lifetime income solution among the plan's investment and/or distribution options.
- Streamlined administration through standardized plan design.
- Clear delineation of fiduciary and administrative responsibilities, ensuring that each plan is managed in the best interests of its participants and beneficiaries, with those responsibilities assumed by benefit and investment professionals rather than participating employers.

Ignoring the retirement coverage gap would do a disservice to millions of hard-working Americans who need help preparing for retirement. Making it easier for small employers to participate in MEPs would go a long way toward righting that wrong.

The Importance of Workplace Retirement Plans

For millions of working Americans, private retirement plans have become the principal means of accumulating the assets they will need, beyond Social Security benefits, to sustain themselves once they exit the workforce. The good news? Those plans are working.

In 1975, just a year after the Employee Retirement Income Security Act (ERISA) was passed, retirement assets per U.S. household, excluding Social Security benefits, averaged $27,300 (in constant, or inflation-adjusted, 2012 dollars).[1] By June 2013, that figure had ballooned to $167,800.[2]

Since then, Americans have continued to bulk up their retirement nest eggs. By September 2014, total U.S. retirement assets stood at $24.2 trillion, up from $469 billion in 1975.[3] Assets in defined contribution retirement savings plans—the type offered by most employers—totaled $6.6 trillion, up from $86 million in 1975. A recent study shows that, at the end of 2012, near-retirees—those between the ages of 60 and 64—had a combined average of nearly $360,000 in their workplace savings plans and Individual Retirement Accounts (IRA).[4]

For many Americans, an employer-sponsored plan such as a 401(k) is the easiest and most economical way to save for retirement. It offers tax benefits, professional

[1] "The Success of the U.S. Retirement System," by Peter Brady, Kimberly Burham and Sarah Holden, the Investment Company Institute, December 2012, Figure 4, pg. 11.

[2] "Our Strong Retirement System: An American Success Story," the American Council of Life Insurers, the American Benefits Council and the Investment Company Institute, December 2013, pg. 5, updating the calculations in "The Success of the U.S. Retirement System," by Peter Brady, Kimberly Burham and Sarah Holden, the Investment Company Institute, December 2012, Figure 4, pg. 11.

[3] Investment Company Institute, "The U.S. Retirement Market, Third Quarter 2014," Table 1.

[4] Fidelity Investments analysis of 990,000 investors having both IRA and workplace retirement savings plan balances at Fidelity as of December 31, 2012. *See* "Fidelity Retirement Savings Analysis Highlights Higher Balances and Contribution Rates of Investors Saving Beyond Workplace Plans," press release, February 28, 2013.

oversight, the convenience of making contributions via payroll deduction, and access to institutional pricing for investment products. Access to a workplace plan doesn't just offer workers an easier way to save for retirement; it also is correlated with better retirement outcomes. Calculations made a few years ago by the Employee Benefit Research Institute (EBRI) found that workers who were earning between $30,000 and $50,000 per year were 16.4 times more likely to save for retirement if they had access to a workplace plan.[5]

More recently, EBRI has documented that among Americans who participate in a retirement plan—a defined contribution plan, a more traditional defined benefit pension plan, an IRA, or some combination of the three—72 percent are somewhat or very confident they and their spouse will have enough money to live comfortably throughout their retirement years. By contrast, only 28 percent of those who do not have a plan are similarly confident of financial security in retirement.[6]

Explanations for why people with access to workplace plans enjoy better outcomes are relatively easy to infer. Workplace plans promote saving and investment by virtue of:

- The employer's endorsement, which may heighten the value of the plan in the eyes of employees.
- The employer's promotion of the plan's benefits, including matching contributions, which can boost plan participation.
- Automatic enrollment and auto-escalation of contributions in the plan, where employers have embraced those design features.
- The ease of making contributions via payroll deduction.

Employees recognize the value these plans offer. In a recent survey of 1,000 401(k) plan participants, nearly 90 percent said a 401(k) is a "must have" benefit.[7]

The Retirement Coverage Gap

The bad news is that while workplace retirement plans are helping tens of millions of working Americans save and invest for retirement, tens of millions more do not have access to a plan at work. This is particularly problematic for workers who are employed by one of the country's many small employers who do not sponsor a plan due to concerns about costs, administrative complexities, and fiduciary liability. The resulting retirement coverage gap is reflected in data compiled by the Bureau of Labor Statistics:

- Eighty-nine percent of workers employed by firms with more than 500 employees, and 78 percent at firms with 100 to 499 employees, have access to retirement plans on the job.[8]
- Only 50 percent of those employed by firms with fewer than 100 workers have access to a workplace retirement plan.[9]

The coverage gap's concentration among small employers is critical because small employers provide jobs for a vast swath of the American populace, particularly among women and multi-ethnic groups. In 2011, private sector organizations with no more than 500 workers employed a total of 65.4 million people, while larger organizations employed 51.5 million. The smaller employers also provided more jobs for women—30.3 million versus 25 million—and for Asian American, American Indian, and Hispanic workers.[10]

The retirement coverage gap has persisted despite a variety of legislative and administrative initiatives that have sought to close it via simplified retirement savings vehicles such as Simplified Employee Pension plans (SEPs), Savings Incentive Match Plans for Employees (SIMPLEs), and voluntary payroll-deduction IRAs.

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[5] Employee Benefit Research Institute estimates from the 2004 Survey of Income and Program Participation Wave 7 Topical Module (2006 data).

[6] Employee Benefit Research Institute, "The 2014 Retirement Confidence Survey," March 2014, Figure 3.

[7] Online survey of 1,000 401(k) plan participants by Koski Research for Schwab Retirement Plan Services between May 27 and June 4, 2014. *See* "Schwab Survey Finds Workers Highly Value Their 401(k) but Are More Likely to Get Help Changing Their Oil than Managing their Investments," Schwab Retirement Plan Services press release, August 19, 2014.

[8] "Employee Benefits in the United States—March 2014," Bureau of Labor Statistics news release of July 25, 2014, pg. 1.

[9] "Employee Benefits in the United States—March 2014," Bureau of Labor Statistics news release of July 25, 2014, pg. 1.

[10] United States Census Bureau, Statistics of U.S. Businesses, 2011 data.

Social Security: A Partial Backstop

Social Security is a critical retirement income backstop for those without a workplace retirement plan. It replaces nearly all of the preretirement income for the lowest quintile of earners after they stop working—87 percent on average—based on inflation-indexed earnings. But for many Americans, Social Security will provide a much smaller fraction of what they need to maintain their standard of living in retirement. Based on an average of their highest 35 years of earnings, earners in the top quintile receiving their first Social Security benefit at age 65 this year can expect it to replace, on average, just 31 percent of their pre-retirement income. Even for medium earners, it will replace only 47 percent.[11]

Multiple Employer Plans: A Potential Solution to the Coverage Gap

Multiple employer plans, or MEPs, offer a promising means of narrowing the retirement coverage gap. A MEP is a type of employee benefit plan that can be maintained as a single plan in which two or more unrelated employers participate. For purposes of this paper, it is a tax-qualified retirement plan.

The MEP concept is not new. MEPs have been allowable under federal tax law and ERISA for decades. However changes are necessary to address impediments limiting the use of MEPs. Current tax law and ERISA rules limit MEP sponsorship primarily to trade associations whose members share a commonality of interest; professional employee organizations (PEOs) that share a co-employer relationship with their clients; and certain large employers who wind up sponsoring MEPs as the result of a corporate restructuring or similar transaction.

As envisioned by a number of members of Congress on both sides of the political aisle, access to MEPs could be broadened, and the plans themselves enhanced, to provide small employers with the economies of scale, administrative simplicity, and limited fiduciary liability they need to be comfortable offering a retirement savings plan to their employees. This idea has been endorsed by the Chamber of Commerce,[12] AARP,[13] numerous affinity organizations, and a number of financial services industry groups, including, among others, the SPARK Institute. In November 2014, the Advisory Council on Employee Welfare and Pension Plans weighed in on MEPs by endorsing Department of Labor action to facilitate MEP formation in its recommendations to the Secretary of Labor.[14]

This paper describes how federal legislators and regulators can help narrow the retirement coverage gap by expanding opportunities for MEP sponsorship and creating a model plan designed specifically for the small business community. In brief, this new breed of MEPs would be open to a diverse universe of smaller employers, managed by identifiable and accountable plan fiduciaries and professionals. The plans would be designed to broaden retirement plan coverage and increase worker savings through the use of automatic enrollment of employees and automatic escalation of their contributions to their plans. Small employers would enjoy the same economies of scale currently enjoyed by larger employers, as well as limited fiduciary liability like those participating in collectively bargained multiemployer plans and association-sponsored multiple employer plans.

Why MEPs, and Why Now?

There is growing recognition at federal and state levels that far too many Americans may not be prepared financially for retirement, that workplace-based retirement savings programs can play a significant role in addressing this problem, and that the need for greater access to workplace retirement programs is greatest among those working for small employers. Legislators have introduced a variety of bills, at both the state and federal levels, that would encourage and/or mandate the offering of a retirement savings program by employers who don't currently sponsor one.

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[11] "Why American Workers' Retirement Income Security Prospects Look so Bleak: A Review of Recent Assessments," Gabo Pang and Sylvester J. Schieber, May 2014, Exhibit 3.

[12] "Private Retirement Benefits in the 21st Century: A Path Forward," U.S. Chamber of Commerce, page 9.

[13] In "The Policy Book: AARP Public Policies 2013–2014," Revised 2014, AARP states in Chapter 4, page 18, "AARP supports the development of model plans that would enable groups of unrelated small employers to pool resources in plans administered and marketed by financial institutions."

[14] *See http://www.dol.gov/ebsa/publications/2014ACreport3.html.*

State initiatives have primarily focused on the possibility of offering state-sponsored retirement plans for employees of private-sector employers. Typically, these plans would require employers who do not otherwise offer a plan to automatically enroll their workers in the state-sponsored plan, under which employee contributions would be invested through an IRA. California was an early mover with the enactment in 2012 of the California Secure Choice Retirement Savings Trust Act. California Secure Choice will require California businesses with five or more employees to defer between 2 and 4 percent of their workers' wages into accounts supervised by a state board.[15] *In January 2015, Illinois enacted legislation that will require employers with at least 25 workers in that state to enroll employees into a new state plan if no other type of plan is being offered.*[16] *Elsewhere, in 2014, the states of Connecticut, Maryland, Minnesota, Oregon, Vermont, and West Virginia began studying the issue of sponsoring retirement plans.*

In Washington, DC, federal legislators have introduced bills that would encourage the use of payroll deduction IRAs, with automatic enrollment, by employers not offering other retirement savings opportunities to their employees.[17] *In addition, the Department of Treasury has been encouraging employers to offer employees access to a new type of Roth IRA, the myRA.*

myRAs are designed to function as low-cost starter retirement savings plans for Americans who may not have access to any other type of retirement program where they work. They will be funded by individual participants, in small increments, through payroll deduction. The sole investment option will be a Treasury savings bond offering the same variable rate of return that federal employees receive when they participate in the Thrift Savings Plan Government Securities Investment Fund, a low-risk vehicle that invests exclusively in a non-marketable short-term U.S. Treasury security. The Treasury Department has created a Web page where individuals can sign up to participate in the myRA program.[18]

While these proposals represent important efforts to make retirement savings programs accessible to more Americans, expanding the role for multiple employer plans would afford employees of small businesses additional, and in some cases more flexible, opportunities to save and invest for retirement no matter where they are located. In contrast to the myRA, for example, small-business MEPs would offer multiple investment options that give participants the flexibility to invest their retirement portfolio in accordance with their own time horizon and tolerance for risk. MEPs also would offer higher contribution limits.[19]

The growing enthusiasm for expanding the role of MEPs reflects a recognition that multiple employer plans would offer small-business employees meaningful opportunities to save and invest for retirement, while minimizing administrative burdens and fiduciary liability for their employers.

Challenges to Expanding MEP Sponsorship and Participation

Expanding access to multiple employer plans for small businesses and their employees will require legislative and regulatory action in Washington. The challenges are concentrated in four areas:

Tax law. Section 413(c) of the Internal Revenue Code already recognizes plans maintained by more than one unrelated employer. However, it imposes a number of requirements on these plans as a condition of maintaining their tax-qualified status. As currently interpreted, some of these requirements, such as nondiscrimination rules, are applied on an employer-by-employer basis rather than a plan basis. This means that just one non-compliant employer can jeopardize the tax status of the entire plan, putting all other employers at risk.

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[15] *See* California Secure Choice Retirement Savings Trust Act, California Senate Bill 1234 at *http://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=201120120SB1234.*

[16] *See* Illinois Secure Choice Savings Program, Public Act 098–1150 (signed January 5, 2015, effective June 1, 2015) at *http://www.ilga.gov/legislation/publicacts/fulltext.asp?Name=098-1150.*

[17] For example, H.R. 5875—SAVE Act of 2014 (113th Congress), H.R. 506 and S. 245—Automatic IRA Act of 2015 (114th Congress).

[18] *https://myra.treasury.gov/individuals.*

[19] As envisioned by this paper, contribution limits for MEPs would be the same as those applicable to 401(k) plans (*i.e.,* $18,000 per employee in 2015). The contribution limit in 2015 for myRAs, like traditional IRAs, is $5,500.

ERISA. For purposes of ERISA, the Department of Labor treats as a single retirement plan only those multiple employer plans that are sponsored by a "cognizable, bona fide group or association of employers" acting in the interest of its members. It also requires that this group of employers have a "commonality of interest," such as operating in the same industry, and exercise either direct or indirect control over the plan. Taken together, these conditions significantly limit the ability of other organizations, such as a local Chamber of Commerce, to sponsor a MEP for a diverse population of smaller employers.

Fiduciary liability. Some employers—particularly small employers—shy away from offering a retirement savings plan because they are concerned about the responsibilities and liabilities they might assume, under ERISA, as plan fiduciaries. The recent uptick in retirement-plan litigation relating to plan fees and other factors has only exacerbated their concerns.

Enforcement. The Labor Department has expressed concern that expanding the number of "open" multiple employer plans—those sponsored by any entity other than "a bona fide group or association of employers"—would allow the promoters of such plans to take advantage of small employers and their employees under the guise of offering a low-cost, no-liability plan.[20]

In the next section of this paper, we'll explore the legislative and regulatory changes needed to make multiple employer plans workable for the small business community, and for the tens of millions of American workers who could benefit from access to them.

The Path to Facilitating Sponsorship and Use of MEPs

To make multiple employer plans accessible to small businesses, lawmakers and regulators will need to take action on several fronts:

Tax law

The IRS or Congress needs to clarify tax law so that any adverse consequences of not complying with the applicable tax-qualification requirements of MEPs will be limited to the noncompliant employer, rather than the entire plan and the rest of its participating employers.[21]

ERISA

Congress and the Department of Labor need to modify ERISA requirements to allow a broader array of entities, organizations, and associations to sponsor MEPs, subject to conditions that will ensure the plans comply with ERISA's fiduciary requirements and minimize risk to plan sponsors and their employees. These conditions might include the following:

- The sponsor must exist for bona fide purposes unrelated to the sponsoring of a retirement plan.
- The documents of the plan must identify the person, or persons, who will serve as the named fiduciary of the plan. That person, or persons, must acknowledge in writing joint and several liability for controlling and managing the operation and administration of the plan.
- The documents of the plan must identify the trustee(s) of the plan responsible for the management and control of the plan's assets, and for the prudent collection of contributions to the plan.
- The documents of the plan must identify the person or persons who will serve as the administrator of the plan, responsible for satisfying reporting, disclosure, and other statutory obligations.
- The plan and plan officials must maintain a fidelity bond, in accordance with ERISA section 412, as well as fiduciary insurance, to safeguard the plan and its participants.

[20] Letter from Phyllis Borzi to Charles Jeszeck, reprinted in "Private Sector Pensions: Federal Agencies Should Collect Data and Coordinate Oversight of Multiple Employer Plans," a GAO Report to the Chairman, Committee on Health, Education, Labor, and Pensions, U.S. Senate, September 2012, pg. 44.

[21] On November 17, 2014, Senators Wyden, Nelson, Brown, Stabenow and Cardin wrote Secretary of the Treasury Jacob Lew urging Treasury to revisit their regulatory position, which discourages multiple employer plans.

- The documents of the plan must ensure that participating employers will not be subject to unreasonable restrictions, penalties, or fees upon ceasing participation in the plan.
- Inasmuch as the retirement coverage gap is most acute among smaller employers, participation in these new MEPs should be limited to those employers with no more than 500 employees. While it is likely that MEPs will appeal principally to employers with 100 or fewer employees, establishing the ceiling at 500 will give small employers ample time to grow without having to worry about identifying a new retirement savings vehicle.

Fiduciary Responsibility

Congress and regulators should consider limiting the fiduciary responsibility of employersparticipating in a MEP to the prudent selection of the MEP sponsor. Similar to the selection of an investment manager under ERISA, such a limitation is not intended to eliminate or reduce fiduciary responsibility with respect to the management and operation of the plan, but rather appropriately allocate those responsibilities to professionals best positioned to protect the interests of plan participants and beneficiaries.

Enforcement

Lawmakers and regulators can help ensure the integrity of MEPs in the marketplace by strengthening the protections afforded plan sponsors and their employees. They can do this by establishing accountability for, and meaningful oversight of, MEPs. Appropriate measures could include:

- A requirement that MEP sponsors file a registration statement with the Department of Labor in advance of offering a retirement plan to employers. The statement could include, among other things, the name of the sponsor; the scope of its intended offering in terms of its geographic area; representations that all applicable conditions, such as those enumerated above, have been satisfied; and copies of the plan documents.
- A requirement that the MEP file an annual report including, in addition to any other information required in its Form 5500 annual report, an audit and a listing of participating employers.[22]
- An amendment to ERISA giving the Department of Labor authority to issue ex parte cease and desist orders as well as summary seizure orders, similar to the authority it already enjoys in overseeing multiple employer welfare arrangements.

A Safe-Harbor Model

To facilitate participation in MEPs and reduce compliance risks for small employers, the Department of the Treasury and the Internal Revenue Service should develop a safe-harbor model plan that minimizes the administrative complexities and costs of MEPs, is not subject to complex tax-qualification testing requirements, and enhances the ability of MEPs to generate positive retirement outcomes for plan participants.

A Model MEP

A model multiple employer plan developed by the Department of Treasury would provide small businesses with a roadmap for plan design and implementation. It would likely incorporate the following features and restrictions:

[22] Congress and the Department of Labor have taken steps to require, for plan years beginning after December 31, 2013, that most multiple employer plans include, as part of the Form 5500 Annual Return/Report, a list of participating employers and a good faith estimate of the percentage of total contributions made by such employers during the plan year. *See* section 104(c) of the Cooperative and Small Employer Charity Pension Flexibility Act (Public Law 113–97, April 7, 2014) adding a new section 103(g) to ERISA. *Also see,* interim final rule amending instructions to the Form 5500 Annual Return/Report at 79 FR 66617 (November 10, 2014).

FEATURES AND CHARACTERISTICS

Segment served	• Small employers. Limit to employers with no more than 500 employees.
Plan structure	• A single plan, with a centrally administered trust, serving all participating employers. • Specifically identified persons who will serve as the named fiduciary, trustee(s), and administrator.
Features	• Funded by employee contributions. • Employer contributions permitted but not mandated. • Subject to contribution limits applicable to 401(k) plans (*i.e.,* $18,000 per employee, plus permissible catch-up contributions, in 2015). • Automatic enrollment of employees at a contribution rate equal to 6 percent of pay, with employees eligible to opt out or select an alternate contribution rate. • Automatic escalation of employee contributions to 10 percent of pay, in annual 1 percent increments, with the opportunity for employees to opt out. • Participant loans not permitted. • Hardship withdrawals permitted only under IRS safe harbor conditions.
Investment and distribution options	• Participants will be offered a broad range of diversified investment options. • In the absence of investment direction, participants initially will be defaulted into an investment option designed to preserve principal, and after 4 years into a qualified default investment alternative such as a target-date fund or balanced fund. • Investment and/or distribution options will include at least one lifetime income product. • Participant accounts may be rolled into an IRA or other qualified retirement plan upon participant's separation from employer.
Fiduciary and administrative responsibilities	• Administrative responsibilities centralized to reduce costs. • Participating employers have limited fiduciary responsibility. • Participants benefit from the applicability of ERISA's fiduciary standards and duties to those responsible for the management of the plan. • Non-discrimination testing not required.

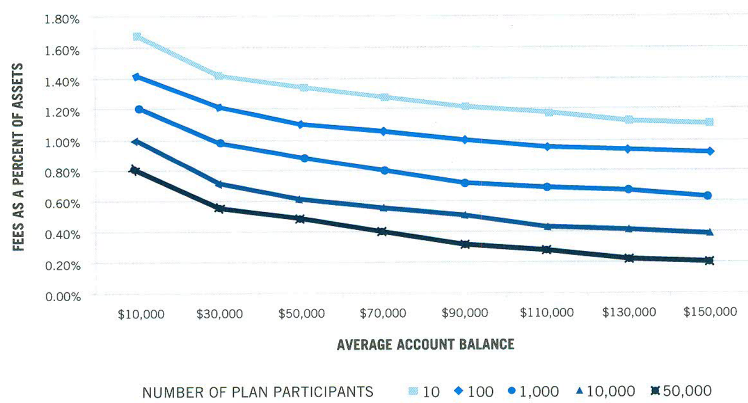
Multiple Employer Plans Will Meet Small Business Objectives

Multiple employer plans designed for the small business community will meet the objectives of small employers who want to help their employees prepare for retirement. As re-envisioned for the small business community, MEPs will:

Reduce costs and administrative burdens. Centralized plan administration and management, along with economies of scale, reduce both administrative burdens and costs—costs that often are borne by the plan's participants and beneficiaries and serve to reduce retirement savings. Exhibit 1 shows how dramatically retirement plan fees fall, as a percentage of plan assets, as the number of participants ina plan increases.

Exhibit 1

PREDICTED FEES AS A PERCENT OF ASSETS BY ACCOUNT SIZE AND NUMBER OF PLAN PARTICIPANTS



Source: "Inside the Structure of Defined Contribution/401(k) Plan Fees, 2013: A Study Assessing the Mechanics of the 'All-In' Fee," conducted by Deloitte Consulting LLP for the Investment Company Institute.

Reduce fiduciary responsibilities for small employers sponsoring retirement plans. Fiduciary and administrative responsibilities will be discharged by plan and investment professionals, thereby enhancing the fiduciary and other protections afforded to employees.

Provide better retirement outcomes for employees. A properly designed MEP will promote saving by employees through the use of automatic enrollment and automatic escalation of their contributions. MEPs may further encourage appropriate investment behavior by providing a choice of investment options selected by investment professionals, better ensuring that plan participants will be able to tailor their portfolios to their investment goals and tolerance for risk. They also will provide enhanced opportunities for cost-effective participant education programs through pooling of resources with other employers. Finally, they will drive positive outcomes by providing participants with access to lifetime income solutions within their plans. Because the ultimate goal of a retirement plan is to allow participants to generate the income they need once they have retired, lifetime income solutions are a critical component of plan design.

Help small businesses compete with larger companies for talent. By giving small businesses a way to help their employees save and invest for retirement in a tax-advantaged plan, small employers will be better equipped to compete with larger employers for talent. Surveys consistently show that workers consider retirement savings plans a valued employee benefit.

Conclusion

Access to a cost-effective, easy-to-use workplace retirement savings program is an important tool for building retirement security. Yet tens of millions of Americans lack access to such a tool. Most in that group are employed by enterprises with 100 or fewer people on their payroll.

Revamping the rules and regulations around multiple employer plans to allow for MEPs that meet the needs and concerns of small employers would help to close the retirement coverage gap and improve the retirement outlook for millions of working Americans. It would give those workers access to professionally managed, institutionally priced retirement programs funded via convenient payroll deduction. And it would help make small employers more competitive with larger employers who can more easily assume the costs and responsibilities associated with sponsoring a retirement plan.

Importantly, incorporating retirement income solutions into MEPs will be crucial to delivering maximum benefits to working Americans. As has become increasingly

clear over the past decade as the first wave of Baby Boomers has begun to exit the workforce, retirement savings plans must function not merely as vehicles for accumulating assets but also as vehicles for converting those assets to income once plan participants have stopped working.

The climate is right for expanding the use of multiple employer plans. This idea is supported by members of Congress in both parties and has won the endorsement of significant interest groups such as the U.S. Chamber of Commerce and AARP.

If you'd like to be part of the effort to expand the role of MEPs for small businesses, or simply learn more about how MEPs can be adapted for the small business marketplace, please contact:

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Additional Resources:

For additional information about improving the private retirement system in the U.S. and retirement outcomes for retirement plan participants, please see these other Prudential white papers:

Guaranteed Lifetime Income and the Importance of Plan Design *http://research.prudential.com/documents/rp/Guaranteed-Lifetime-Income-and-the-Importance-of-Plan-Design.pdf?doc=GuaranteedLifetimeIncome&bu=ret&ref=PDF&cid=MEP*

Overcoming Participant Inertia: Automatic Features that Improve Outcomes While Improving Your Plan's Bottom Line *http://research.prudential.com/documents/rp/Automated_Solutions_Paper-RSWP008.pdf?doc=OvercomingParticipantInertia&bu=ret&ref=PDF&cid=MEP*

Innovative Strategies to Help Maximize Social Security Benefits *http://research.prudential.com/documents/rp/InnovativeSocialSecurityNov2012.pdf?doc=innovativestrategies1112&bu=ret&ref=PDF&cid=MEP*

Planning for Retirement: The Importance of Workplace Retirement Plans and Guaranteed Lifetime Income *http://research.prudential.com/documents/rp/nrri-december-2014.pdf?doc=NRRIDec2014PDF&bu=ret&ref=PDF&cid=MEP*

QUESTIONS SUBMITTED FOR THE RECORD TO JOHN J. KALAMARIDES

QUESTIONS SUBMITTED BY HON. ORRIN G. HATCH

Question. Mr. Kalamarides, you mentioned part-time workers in your testimony. The working group identified proposals that would target "long-term" part-time workers, so-called "career part-time" workers who spend 3 or more years in part-time status working for the same employer. As more workers spend lengthy portions of their careers in part-time employment, this seems like an issue that needs to be explored. What are the obstacles to such coverage today, and are they primarily legal or economic in nature?

Answer. We agree with the recommendations of the Savings and Investment Working Group that more needs to be done to extend retirement savings opportunities to the so-called "career part-time" worker, as well as self-employed "Gig Economy" workers. The Savings and Investment Working Group estimates that 37 percent of part-time workers do not have access to a retirement plan. Alan Kruger and the Brookings Institute estimate 600 thousand workers are solely employed by the new gig economy. While extending participation opportunities in employer-sponsored retirement plans may be the most viable option for some part-time workers, we believe further dialogue with the plan sponsor community is needed to better understand potential administrative and cost impediments of including such workers in existing plans. We also believe that, with respect to both part-time and self-employed workers, consideration should be given whether an Open MEP-like plan, offering a 401(k) savings rates along with low administrative fees and institutional investments represents a potentially viable retirement saving opportunity for non-traditional workers outside the ERISA-coverage framework.

We welcome the opportunity to further explore these issues with the committee.

Question. Mr. Kalamarides, you mentioned in your testimony that the Department of Labor recently published guidance to facilitate State sponsorship of MEPs. The guidance does not resolve the tax qualification issues you discussed, which, of course, are in the jurisdiction of this committee. Despite the shortcomings of the guidance in this regard, and without asking you to comment on the wisdom of State-sponsored MEPS, do you believe that the Open MEP can co-exist alongside state-sponsored MEPS in those States that choose to set up MEPS?

Answer. We believe that both state-sponsored and private sector-sponsored Open MEPs can co-exist, if—and only if—there is a level playing field; that is, rules and regulations governing MEPs do not tip the scales in favor of state-sponsored arrangements. A level playing field, in our view, would require that a State opting to sponsor a MEP would act as both the name fiduciary and the administrator of the MEP. In addition, the State, consistent with ERISA's "prudence" and "solely in the interest" requirements would be responsible for the selection and monitoring of plan investments and service providers to the MEP. In addition, a state-sponsored MEP would be required, consistent with ERISA, to be trusteed and, the trustee, would be responsible for monitoring and timely collection of participant contributions. A level playing field, in our view, would ensure a robust marketplace in which a state-sponsored MEP could complement private sector MEP coverage opportunities, all to the benefit of the small employer community.

Question. Mr. Kalamarides, in your testimony you said that you support the Open MEP to encourage businesses to set up 401(k) plans. You also point out that 401(k) MEPs offer greater opportunities for workers to save for retirement than workplace IRA programs because of the higher contribution levels available in 401(k) plans. The administration announced this week that it supports Open MEPs as well as workplace-based IRA programs. We're still waiting for all the details, but the administration seems to want workplace IRA programs to be mandatory for employers that do not already sponsor a plan. It would be quite a challenge, to say the least, to pass a new employer mandate in Congress. What do you think of *voluntary* workplace IRA programs, and do you think a voluntary workplace IRA program also could be organized as an Open MEP?

Answer. Pursuant to Department of Labor regulations [1] and interpretive guidance,[2] employers have long been able to offer their employees the opportunity to save at the workplace through a payroll deduction IRA program, without implicating the compliance burdens and costs imposed on ERISA-covered plans; however, few have opted to do so. A number of States have focused on IRA-based programs primarily in an effort to avoid ERISA coverage. We believe that Open MEPs represent the most viable and most effective means by which to extend meaningful savings opportunities to the millions of workers without access to workplace based savings programs. As noted in my testimony, an Open MEP 401(k) plan would permit employees to save at a rate of up to $18,000 per year, as compared to the maximum contribution rate of $5,500 for a traditional IRA in 2015. An Open MEP, in addition to lower administrative and investment costs, could permit matching employer contributions further enhancing retirement savings opportunities for employees. And, unlike IRAs, employees participating in an Open MEP would enjoy the Federal protections accorded by ERISA. As efforts continue at both the State and Federal level to move IRA-based arrangements forward, we believe working Americans deserve access to more meaningful retirement savings opportunities, namely access to an Open MEP with traditional 401(k) benefits. For that reason, we encourage members of Congress to move quickly to provide a meaningful Federal solution and enact legislation that will foster and promote MEP sponsorship and participation.

Question. Mr. Kalamarides, in your testimony you recommended that, in framing legislation that would expand MEP sponsorship and participation, consideration should be given to setting forth a model Open MEP plan or directing Treasury, IRS and Labor to work together to develop such a model. What provisions, in your view, should be included in such a model plan?

Answer. First, we believe that a model plan—a plan that would not be subject to the burdensome and costly discrimination and other testing currently applicable to retirement plans—will encourage employer participation through reduced costs and risks and will enhance employee retirement preparedness through increased participation and savings rates. A model plan that is widely adopted may also reduce costs for employers moving from one MEP to another and may reduce barriers

[1] *See* 29 CFR § 2510.3–2(d).
[2] *See* 29 CFR § 2509.99–1.

for employee portability. To accomplish these objectives, we believe a model plan should provide for:

- Specific identification, in plan documents, of the person or persons who will serve as the plan's named fiduciary, as well as the trustee or trustees responsible for the management of the plan's assets and the prudent collection of employee contributions to the plan.
- Specific identification, in the plan documents, the person or persons who will serve as the plan's administrator, responsible for compliance with ERISA's reporting and disclosure requirements.
- Automatic enrollment of employees at a contribution rate equal to 6%, with a right to opt out of the plan or elect a different contribution rate.
- Automatic escalation of employee contributions up to 10 percent of pay.
- A broad range of investment alternatives, consistent with the standards set forth in the Department of Labor's regulations under section 404(c) at 29 CFR § 2550.404c–1.
- At least one investment alternative or distribution option that includes a lifetime income product—far too few employees currently have access to lifetime income through their retirement plan.
- A default investment alternative that, for the first 4 years of participation, is designed to preserve principal. After 4 years, and in the absence of a participant's direction to the contrary, contributions would be transmitted to a Qualified Default Investment Alternative (QDIA), consistent with the Department of Labor's regulation at 29 CFR § 2550.404c–5. By utilizing a preservation of principal investment as the initial default investment, newer participants are largely protected from market volatility that could discourage continued participation or reduce savings rates during the early savings years.
- Hardship withdrawals, but not participant loans; thereby reducing the likelihood of leakage from the system.

While we believe most Open MEPs would gravitate to a model, we believe that, in the interest of not discouraging innovation and creativity, use of a model plan structure should be voluntary and not a mandate for all Open MEPs.

Thank you and we look forward to working with the committee on this important issue.

QUESTIONS SUBMITTED BY HON. DEAN HELLER

Question. What is the most important thing lawmakers can do right now to help small businesses offer a workplace savings plan to their employees?

Answer. We believe removing the current ERISA and tax impediments to MEP sponsorship and participation would represent an important first step in helping small employers offer workplace savings to their employees. We also believe that, given the bipartisan support for MEPs in both the Senate and the House, as well as support from consumer advocates and the administration, an Open MEP legislative fix is achievable in the short-term. Lack of access to retirement savings opportunities in the workplace is an immediate problem for millions of working Americans. Today there is widespread, bipartisan support for a solution—Open MEPs; we believe the time is now for Congress and the administration to act on this critical issue. We look forward to working with you and your staff to make this happen.

Question. As you know, current law provides a tax credit of up to $500 per year, for 3 years, for start-up costs related to qualified small employer plans. However, the uptake rate for this credit has been historically weak. Why do you think the uptake has been so low?

Answer. While a tax credit may help mitigate some of the initial start up cost concerns for some employers, we believe that the administrative, fiduciary, and tax qualification responsibilities and liabilities attendant to sponsoring a standalone retirement plan, may be too daunting for far too many small employers; employers who are otherwise committed to doing the right thing for their employees. In 2015, Prudential surveyed 850 small businesses without plans and found there are three barriers to adoption—cost, administrative hassle and fiduciary responsibilities. In the same survey, we found demand for 401(k) plans would increase by 250 percent

by removing these barriers. As indicated in my testimony, we believe that Open MEPs offer a low cost, low risk means by which today's smaller employers can offer their employees a meaningful opportunity to save for retirement. An Open MEP 401(k) would permit employees to save a rate of up to $18,000 per year, as compared to the maximum contribution rate of $5,500 for a traditional IRA in 2015. An Open MEP also enables smaller employers to enjoy economies of scale, resulting in lower administrative and investment costs. An Open MEP also affords smaller employers the opportunity to reduce their fiduciary responsibilities and liabilities by transferring—not eliminating—those responsibilities and liabilities to benefits professionals who are best positioned to operate the plan in a manner consistent with ERISA and the interests of the employees.

Question. I am deeply concerned with leakage. In my home State, we have felt the pressures of the recession and many of the constituents have had to dip into their retirement funds to make ends meet. In your opinion, what is the single best way we as lawmakers can make it easier for workers to return assets for retirement accounts after they have been withdrawn?

Answer. Studies have suggested that "leakage"—any preretirement withdrawal that permanently removes money from a retirement saving program—can dramatically reduce a person's retirement readiness. One the major causes of leakage is participant loans. About 90 percent of participants in 401(k) plans can borrow from their plan account. However, borrowed amounts reduce potential investment gains and have to repaid with after tax dollars. Moreover, failures to repay loans in a timely manner can result in taxation on the outstanding balance, as well as early withdrawal penalties. For these reasons, we have recommended that, in connection with the development of an Open MEP model plan that loans not be permitted. Loan programs can be expensive to administer and, as noted, can place retirement savings at risk. However, recognizing that limited access to retirement savings may be necessary for some employees, a model Open MEP plan could permit "hardship" withdrawals, but preferably only those permitted under the IRS safe harbor conditions (such as, payment of medical expenses, payments to prevent eviction, funeral expenses, repair of principal residence, *etc.*).

Question. I strongly believe that tax reform, done the right way, can improve our fiscal picture. What steps can we as lawmakers take to improve our retirement savings in a fiscally responsible way?

Answer. As has become clear through recent efforts, tax reform is a complex undertaking which often leads to unintended consequences. As Congress continues to grapple with how to make our tax system a driver for domestic economic growth and more competitive globally, there are both opportunities and risks. A number of tax reform proposals have focused on reducing or capping retirement-related expenditures. Without addressing or recommending any particular proposal, we do encourage lawmakers to reallocate, in part, any tax reform savings attributable to reductions in retirement-related expenditures to expanding retirement coverage and savings opportunities for lower and middle income earners. But we also caution against inadvertently raising retirement product affordability by indirectly raising the costs on retirement product providers through inappropriate company taxation.

Question. I understand the President is expected to propose an Open-MEP plan in his FY17 budget. I would imagine a significant amount of implementing guidance would be needed. If open-MEPs were expanded, what role, if any, would the IRS play in this additional guidance?

Answer. We do not believe that the legislative proposals introduced to date, or the administration's proposal, relating to Open MEPs, necessarily require implementing regulatory or other guidance from the Agencies (Treasury, IRS or Labor) and we would encourage members, as they consider legislation to promote Open MEPs, to keep the need for regulatory guidance to a minimum. In this regard, we are concerned that the need for implementation guidance will, given the protracted nature of the regulatory process and the potential for competing agency priorities, unnecessarily delay the offering of Open MEPs for several years.

With regard to your specific question, we have two suggestions. First, to the extent not specifically addressed in legislation, Treasury and the IRS will need to provide guidance addressing the tax qualification issues that put both a MEP and other participating employers potentially at risk due to the acts of one noncompliant participating employer—often referred to as the "one bad apple" rule.

Second, we believe that Treasury and IRS, working in coordination with the Department of Labor, should be directed to develop a model Open MEP plan—a plan

that would not be subject to the burdensome and costly discrimination and other testing currently applicable to retirement plans and that will encourage employer participation through reduced costs and risks. A properly designed model plan will also encourage increased participation and savings rates for employees through the use auto-features. A model plan that is widely adopted may also reduce costs for employers moving from one MEP to another and may reduce barriers for employee portability. In our view, these objectives could be accomplished through a model plan that provides for:

- Specific identification, in plan documents, of the person or persons who will serve as the plan's named fiduciary, as well as the trustee or trustees responsible for the management of the plan's assets and the prudent collection of employee contributions to the plan.
- Specific identification, in the plan documents, the person or persons who will serve as the plan's administrator, responsible for compliance with ERISA's reporting and disclosure requirements.
- Automatic enrollment of employees at a contribution rate equal to 6%, with a right to opt out of the plan or elect a different contribution rate.
- Automatic escalation of employee contributions up to 10 percent of pay.
- A broad range of investment alternatives, consistent with the standards set forth in the Department of Labor's regulations under section 404(c) at 29 CFR § 2550.404c–1.
- At least one investment alternative or distribution option that includes a lifetime income product—far too few employees currently have access to lifetime income through their retirement plan.
- A default investment alternative that, for the first 4 years of participation, is designed to preserve principal. After 4 years, and in the absence of a participant's direction to the contrary, contributions would be transmitted to a Qualified Default Investment Alternative (QDIA), consistent with the Department of Labor's regulation at 29 CFR § 2550.404c–5. By utilizing a preservation of principal investment as the initial default investment, newer participants are largely protected from market volatility that could discourage continued participation or reduce savings rates during the early savings years.
- Hardship withdrawals, but not participant loans; thereby reducing the likelihood of leakage from the system.

While we believe most Open MEPs would gravitate to a model, we believe that, in the interest of not discouraging innovation and creativity, use of a model plan structure should be voluntary and not a mandate for all Open MEPs.

Thank you, and we look forward to working with the committee on this important issue.

Question. Like many Nevadans, I am a strong supporter of ways to help our vulnerable populations save long-term for our retirement. What is the single most important thing lawmakers can do right now to help low-income and moderate-income families prepare for retirement?

Answer. As with your Question 1, we believe removing the current ERISA and tax impediments to MEP sponsorship and participation would represent an important first step in helping low and moderate income families prepare for retirement. According to data from the nonprofit, Employee Benefit Research Institute, people earning between $30,000 and $50,000 per year are 16.4 times more likely to save for retirement if they have access to a workplace retirement plan. Unfortunately, tens of millions of working Americans do not have access to a plan on the job, leaving far too many unprepared to meet their financial needs after they stop working. This retirement coverage gap is most acute among employees of small companies, many of whom do not sponsor plans due to concerns about costs, complexity and fiduciary liability. The lack of coverage is especially problematic for the 30 million women, 12 million Latinos, 6 million African Americans and 4 million Asian Americans that work at small business. Open MEPs represent a bipartisan solution to addressing this critical retirement coverage issue.

We look forward to working with you on this issue so critical to millions of working Americans.

QUESTIONS SUBMITTED BY HON. MARIA CANTWELL

Question. I have long been a proponent that we should encourage guaranteed lifetime income options, including annuity products, as a part of our retirement security agenda. Prudential, in its written testimony, recommended that a safe-harbor model plan be developed by Treasury, the IRS and the Department of Labor to encourage participation in open multi-employer plans. It is also recommend that this model plan include an investment or distribution option that includes a lifetime income plan.

Why do you believe including a guaranteed lifetime income option in this mix is so important?

Answer. With an estimated 10,000 Americans reaching retirement age every day, we know that very few of those individuals are being afforded the opportunity to consider a guaranteed lifetime income option as part of their retirement plan. We also know that few of today's workers are able to manage investment and longevity risks in retirement on their own. As recognized by the Council of Economic Advisers' February 2, 2012 report, *Supporting Retirement for American Families,* this is a particularly significant issue for women, who tend to have lower retirement saving rates than men, while having longer life expectancies. Guaranteed lifetime income products provide a means by which all workers can enjoy both certainty and security during their retirement years. We believe a model Open MEP plan with at least one investment or distribution option that includes a lifetime income solution would be a promising start to introducing both employers and their employees to the benefits of a guaranteed lifetime income option.

Question. Do you believe Congress should provide more direction regarding the composition of a model plan?

Answer. Yes. We believe the Department of the Treasury, Internal Revenue Service and the Department of Labor would benefit from Congressional direction regarding the composition of a model Open MEP plan. In this regard, we believe such direction should the required development of a model plan that provides for:

- Specific identification, in plan documents, of the person or persons who will serve as the plan's named fiduciary, as well as the trustee or trustees responsible for the management of the plan's assets and the prudent collection of employee contributions to the plan.
- Specific identification, in the plan documents, the person or persons who will serve as the plan's administrator, responsible for compliance with ERISA's reporting and disclosure requirements.
- Automatic enrollment of employees at a contribution rate equal to 6%, with a right to opt out of the plan or elect a different contribution rate.
- Automatic escalation of employee contributions up to 10 percent of pay.
- A broad range of investment alternatives, consistent with the standards set forth in the Department of Labor's regulations under section 404(c) at 29 CFR § 2550.404c–1.
- At least one investment alternative or distribution option that includes a lifetime income product—far too few employees currently have access to lifetime income through their retirement plan.
- A default investment alternative that, for the first 4 years of participation, is designed to preserve principal. After 4 years, and in the absence of a participant's direction to the contrary, contributions would be transmitted to a Qualified Default Investment Alternative (QDIA), consistent with the Department of Labor's regulation at 29 CFR § 2550.404c–5. By utilizing a preservation of principal investment as the initial default investment, newer participants are largely protected from market volatility that could discourage continued participation or reduce savings rates during the early savings years.
- Hardship withdrawals, but not participant loans; thereby reducing the likelihood of leakage from the system.

While we believe most Open MEPs would gravitate to a model, we believe that, in the interest of not discouraging innovation and creativity, use of a model plan structure should be voluntary and not a mandate for all Open MEPs.

Question. Another important lifetime income issue we've looked at concerns portability of lifetime income products. Younger and lower-income workers actively sav-

ing for their retirements have to worry about transferring those balances to new plans when changing jobs. The issue of leakage and lost accounts for these workers during the transfer—often because of their smaller dollar balances—results in a disproportionate impact when lost. These are Americans who need more retirement savings than most. This issue has been highlighted by the President, the Department of Labor, and here in Congress. What partnerships exist in making sure that the technology and support also exists in ensuring that we eliminate this ongoing problem?

Answer. We recognize that the combination of plan terminations and a highly mobile workplace can create challenges for both workers and employers in terms of tracking benefit entitlements. With the enactment of the Pension Protection Act of 2006, the Pension Benefit Guaranty Corporation (PBGC) was vested with the authority for collecting and maintaining information for missing defined contribution plan participants. We believe the PBGC continues to represent the single best source for missing participant-related information. Accordingly, we are encouraged by efforts of the PBGC and the administration to implement a program to assist defined contribution plan participants in locating their accounts.

Question. I've worked on legislation along the lines of the recommendations in your testimony on developing policies to ensure lifetime income portability and annuity selection safe harbors. Why are these provisions important?

Answer. As recognized by the Savings and Investment Working Group, defined contribution plans should be encouraged to offer annuities or other installment products as investment options, thereby, enabling employees to invest in these products gradually over their careers. However, changes in providers or investment offerings can put an employee's investment in such products and options at risk. While innovation is taking place in the marketplace to mitigate such risks, we strongly support a legislative solution that would permit the distribution of the investment to the employee via a plan-to-plan transfer to another employer-sponsored plan or to an IRA, without regard to whether a distribution would otherwise be permitted. Such a legislative solution was included in S. 1270, introduced by Senator Hatch in the 113th Congress and is consistent with the recommendations of the Saving and Investment Working Group. We also are encouraged by the administration's inclusion of similar proposals in its 2016 and 2017 Budget documents.

In addition to lifetime income portability, we support the recommendations of the Savings and Investment Working Group relating to changes to the rules governing the selection of annuity providers. In 2010 the Departments of Labor and Treasury solicited public comment and held hearings on improving defined contribution plans. One of the key takeaways from that joint agency initiative was that the current rule governing the selection of annuity providers—a safe harbor intended to encourage the inclusion of annuities in defined contribution plans—is not working. Of particular concern is that part of the rule that requires any employer considering the inclusion of an annuity product to assess, and assume fiduciary liability for, the ability of the annuity provider to satisfy its contractual obligations.

While we recognize the importance of such determinations, we believe the burden of such assessments is appropriately the role of State insurance regulators, not plan fiduciaries. In our experience, while most plan fiduciaries are comfortable making determinations relating to the reasonableness of costs in relation to benefits and the quality of services, few are comfortable determining the long-term financial viability of an insurer or other financial institution. For this reason, we believe the current safe harbor standard is having a chilling effect on plan sponsor considerations of guaranteed lifetime income products and new standards, like those identified by the Savings and Investment Working Group, are very much needed. With 10,000 individuals reaching retirement age each day, access to guaranteed lifetime income solutions is an issue that needs to be addressed soon.

Thank you, and we would welcome the opportunity to work with the committee on this important issue.

Question. In 2015, Washington State became one of the first States in the country to authorize a Small Business Retirement Marketplace, to make it easier and less expensive for small businesses to offer retirement savings options to their employees. Under Washington's program, employers with fewer than 100 employees will be able to voluntarily participate in this marketplace and offer low-cost retirement savings plans, which are portable, to their employees. Do you believe that this type of marketplace will increase small business participation and make it easier for them to offer a retirement plan for their employees? What is the impact on employ-

ees' savings rates when their employer offers a retirement plan compared to those who do not?

Answer. Washington State's marketplace approach to expanding retirement coverage is an excellent example of how States can, through a voluntary process, increase employer awareness of and access to retirement savings opportunities for their employees. We believe a Federal solution—namely, Open MEPs—is a necessary complement to the efforts of States like Washington. While improved access to retirement savings programs is an important step, our research indicates that many employers, particularly smaller employers, will continue to have concerns about the administrative complexities, costs, and fiduciary liability attendant to maintaining a standalone plan. Open MEPs represent a means by which to address these issues, but legislative action is necessary to expand MEP sponsorship and participation. We support the recommendations of the Savings and Investment Working Group and look forward to working with you and other members in moving such legislation forward.

QUESTION SUBMITTED BY HON. BENJAMIN L. CARDIN

Question. There are many existing proposals to improve our retirement system. You mention several in your testimony that could increase access to retirement savings as well as increase the amount of savings for those who participate in retirement plans. These are incredibly important issues, and I hope that our committee can take up commonsense, bipartisan proposals to address them. That being said, while the focus of retirement policy is often rightly on access and accumulation, distribution of retirement benefits over the life of retirees is also very important. In your view, what steps can we take to encourage lifetime income security? Aside from the suggestions contained in the Savings and Investment Working Group report, are there any other problems, concerns, or reforms that we should consider to address lifetime income and decumulation issues?

Answer. We believe far too many working Americans do not have access to guaranteed lifetime income solutions and far too many of our retirees are inadequately prepared to manage investment and longevity risks during their retirement years. In our view, these issues could be addressed through three regulatory and/or legislative actions. First, plan sponsors must be willing to include guaranteed lifetime income products as part of their retirement plan investment and/or distribution options. The primary impediment to including such offerings as part of a defined contribution plan is the fiduciary liability attendant to the selection and monitoring of annuity providers. This fact was well established by the Department of Labor and the Department of the Treasury in 2010 during 2 days of hearings on lifetime income issues. Efforts to address this problem through changes to Labor's current annuity selection safe harbor have not developed. We commend the Savings and Investment Working Group for their support for safe harbor changes; changes that recognize the challenges for plan sponsors in having to assess the financial capability of an insurer to satisfy its long term financial commitments, assessments typically reserved to insurance experts in State regulatory agencies. We believe that adoption of the proposals identified by the Savings and Investment Working Group would represent a major step forward for plan sponsor inclusion of guaranteed lifetime income solutions in their plans.

Second, we need to ensure that participants, through lifetime income disclosures, understand how their account balances translate into a lifetime income stream. In this regard, we commend the efforts of Senators Isakson and Murphy for their work in moving lifetime income disclosure legislation forward. We believe clarifying the means by which plan sponsors can provide lifetime income disclosures without unnecessarily increasing fiduciary and plan liability for such disclosures would dramatically increase the offering of such disclosures; ultimately resulting in better informed plan participants.

Lastly, we need to ensure that participants have the information they need to make informed decisions regarding their distribution options and the challenges attendant to managing investment and longevity risks during their retirement years. The guidance provided by the Department of Labor in 1996 (Interpretive Bulletin 96–1) clarifying the type and form of investment-related information plan sponsors can provide their employees without such information being considered "investment advice" has helped millions of plan participants to make more informed investment decisions within their 401(k) plans. We believe similar guidance, regulatory or statutory, is necessary to encourage and promote the furnishing of educational materials

and programs relating to understanding available distribution options and preparing for one's retirement years. We would welcome the opportunity to work with you and other members to ensure that the principles of Interpretive Bulletin 96–1 are preserved and expanded to include education relating to the decumulation phase.

QUESTIONS SUBMITTED BY HON. ROBERT MENENDEZ

Question. Mr. Kalamarides, in your testimony you recommended that, in framing legislation that would expand MEP sponsorship and participation, consideration should be given to setting forth a model Open MEP plan or directing Treasury, IRS and Labor to work together to develop such a model. Would you share your thoughts on what should be included in such a model plan?

Answer. Thank you for the question. First, we believe that a model plan—a plan that would not be subject to the burdensome and costly discrimination and other testing currently applicable to retirement plans—will encourage employer participation through reduced costs and risks and will enhance employee retirement preparedness through increased participation and savings rates. A model plan that is widely adopted may also reduce costs for employers moving from one MEP to another and may reduce barriers for employee portability. To accomplish these objectives, we believe a model plan should provide for:

- Specific identification, in plan documents, of the person or persons who will serve as the plan's named fiduciary, as well as the trustee or trustees responsible for the management of the plan's assets and the prudent collection of employee contributions to the plan.
- Specific identification, in the plan documents, the person or persons who will serve as the plan's administrator, responsible for compliance with ERISA's reporting and disclosure requirements.
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- Hardship withdrawals, but not participant loans; thereby reducing the likelihood of leakage from the system.

While we believe most Open MEPs would gravitate to a model, we believe that, in the interest of not discouraging innovation and creativity, use of a model plan structure should be voluntary and not a mandate for all Open MEPs.

Thank you, and we look forward to working with the committee on this important issue.

Question. Mr. Kalamarides, in your testimony you make reference to the fact that far too many working Americans do not have access to guaranteed lifetime income, leaving them on their own to manage investment and longevity risks—which we know few are qualified to do. Do you have suggestions as to how we might improve this situation?

Answer. Thank you for the question; you raise a very significant question for today's workers and an issue recognized by your committee's Savings and Investment Working Group.

Prudential supports approaches identified by the Working Group pursuant to which plan fiduciaries would, on questions of financial viability, look to insurers to confirm they are in good standing with State licensing, financial solvency, auditing and reporting requirements; requirements established by the States to protect their citizens, including plan participants.

In 2010 the Departments of Labor and Treasury solicited public comment and held hearings on improving defined contribution plans. One of the key takeaways from that joint agency initiative was that the current rule governing the selection of annuity providers—a safe harbor intended to encourage the inclusion of annuities in defined contribution plans—is not working. Of particular concern is that part of the rule that requires any employer considering the inclusion of an annuity product to assess, and assume fiduciary liability for, the ability of the annuity provider to satisfy its contractual obligations.

While we recognize the importance of such determinations, we believe the burden of such assessments is appropriately the role of State insurance regulators, not plan fiduciaries. In our experience, while most plan fiduciaries are comfortable making determinations relating to the reasonableness of costs in relation to benefits and the quality of services, few are comfortable determining the long-term financial viability of an insurer or other financial institution. For this reason, we believe the current safe harbor standard is having a chilling effect on plan sponsor considerations of guaranteed lifetime income products and new standards, like those identified by the Savings and Investment Working Group, are very much needed. With 10,000 individuals reaching retirement age each day, access to guaranteed lifetime income solutions is an issue that needs to be addressed soon.

Thank you, and we would welcome the opportunity to work with the committee on this important issue.

PREPARED STATEMENT OF ALICIA H. MUNNELL, PH.D., PETER F. DRUCKER PROFESSOR OF MANAGEMENT SCIENCE, CARROLL SCHOOL OF MANAGEMENT, AND DIRECTOR, CENTER FOR RETIREMENT RESEARCH, BOSTON COLLEGE *

Chairman Hatch, Ranking Member Wyden, and members of the committee, thank you for the opportunity to testify today about "The Savings and Investment Bipartisan Tax Working Group Report."

This testimony underlines the importance of the Working Group's recommendations to broaden coverage and encourage retirement saving by lower-paid workers. But it also argues that we are facing an enormous retirement income challenge and therefore need even bolder changes.

This testimony proceeds as follows. The first section describes the retirement landscape, where more than half of working-age households are at risk of inadequate retirement income.[1] The second section discusses the extent to which the Working Group's proposals—which focus on the coverage gap and contributions by lower-paid workers—would ameliorate the situation. The third section recommends some broader solutions: (1) make 401(k) plans automatic and reduce leakage; and (2) enact national auto-IRA legislation. The final section concludes that the Senate Finance Committee could make an enormous contribution to heading off the coming crisis.

THE COMING RETIREMENT CRISIS

To address the adequacy of retirement preparedness, the Center that I direct has developed a National Retirement Risk Index (NRRI), which relies on data from the Federal Reserve's *Survey of Consumer Finances*.[2] The NRRI compares projected replacement rates for working households ages 30–59 to target replacement rates that permit them to enjoy the same consumption in each period before and after retirement (see Figure 1). The Index measures the percentage of all households that fall more than 10 percent below their target.

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* The views expressed are solely those of the author and do not represent the views or policy of the Center for Retirement Research at Boston College.

[1] For more details, see Ellis, Munnell, and Eschtruth (2014).

[2] For details on the NRRI methodology, see Munnell, Hou, and Webb (2014).

The most recent NRRI results show that about half of all households are at risk, up from about 30 percent in 1983 (see Figure 2). So the problem is widespread and is getting worse over time.

Why do we have such a serious retirement income problem today when recent generations have retired in relative comfort? The reason is that baby boomers—and those who follow—will face a much different retirement landscape than their parents. The problem is twofold: (1) households will need more retirement income; and (2) they will receive less support from the traditional sources of Social Security and employer-sponsored plans. And today, as in the past, half of private sector workers do not participate in any type of retirement plan at a given point in time.

The Need for Retirement Income Is Growing

Today's workers will need more income when they retire because retirement spans are getting longer, health care costs are rising, and interest rates are very low.

Turning first to retirement spans. The number of years spent in retirement depends both on when people retire and how long they live in retirement. After declining for many decades, in the mid-1980s the average retirement age stabilized and then gradually increased from 62 to 64 for men. However, the latest evidence shows little change in average retirement ages over the past several years, suggesting the trend toward later retirement may be running out of steam.[3] Meanwhile, life expectancy at 65 is continuing to rise steadily (see Table 1). On balance, the retirement period has been getting longer over time, from 13 years in 1960 to about 20 years today (see Figure 3).

Second, while retirees have health insurance coverage through Medicare, they still face substantial out-of-pocket costs for premiums (Parts B and D), deductibles, copayments, and routine health services that are not covered by Medicare. Part B out-of-pocket costs alone have more than doubled since 1980, accounting for 15 percent of the average Social Security benefit today (see Figure 4). For individuals who require more than a brief stay in a nursing home, long-term care costs represent an additional expense.

Third, real interest rates have fallen dramatically over the past two decades, and today's rates continue to hover around historic lows of 1 percent (see Figure 5). Therefore, retirees need a much bigger nest egg than in the past to generate a given amount of income.

These factors combined mean that people are going to need to accumulate substantially more retirement income now than in the past.

Traditional Sources of Retirement Income Are Providing Less Support

At the same time that people need more retirement income, traditional sources are shrinking. Both Social Security and employer-sponsored retirement plans will provide less support than in the past. This trend is especially worrisome because people save virtually nothing outside of these two vehicles.

Social Security. Social Security benefits are the foundation of the retirement income system. But, under current law, these benefits are already shrinking in their ability to replace pre-retirement income for three reasons.

First, the gradual rise in the program's "Full Retirement Age" from 65 to 67 is cutting benefits across the board. For those who continue to retire at 65, this cut takes the form of lower monthly benefits; for those who choose to work longer, it takes the form of fewer years of benefits. For the typical earner who retires at 65, the replacement rate will drop from about 40 percent today to 36 percent once the transition is complete.

Second, Medicare premiums, which are automatically deducted from Social Security benefits, are rising faster than benefit levels. As a result, Part B premiums alone are estimated to increase from 5.4 percent of the average Social Security benefit for someone retiring in 1990 to 10.4 percent for someone retiring in 2030.

Third, more benefits will be subject to taxation under the personal income tax. Individuals with more than $25,000 and married couples with more than $32,000 of "combined income" pay taxes on up to 85 percent of their Social Security benefits. In 1985, only about 10 percent of beneficiaries had to pay taxes on their benefits, but the percentage of people subject to tax has been increasing over time because these thresholds are not indexed for growth in average wages or even inflation.

[3] Munnell (2015).

Today, almost 40 percent of households pay taxes on their benefits, and by 2030 more than half of households are expected to be subject to this tax.

The combined impact of these factors will reduce Social Security replacement rates for the average worker retiring at 65 by nearly a quarter—from a net 40 percent in 1985 to 30 percent by 2030 (see Figure 6).

And these reductions are happening without any changes in current law. If benefits are cut back further to address Social Security's long-term financial shortfall, replacement rates will drop even more.

Employer-Sponsored Retirement Plans. With declining replacement rates from Social Security, employer-sponsored retirement plans become much more important.

For those lucky enough to work for an employer providing a retirement plan, the nature of these plans has changed dramatically from defined benefit plans to 401(k)s. This shift means that the employee rather than the employer makes all the decisions *and* bears all the risks. Not long after the advent of 401(k) plans, it became clear that participants were accumulating only modest balances in these accounts.

As a result, in 2006 policymakers tried to make 401(k)s function more effectively through the Pension Protection Act (PPA). The PPA encouraged 401(k) plan sponsors to adopt automatic mechanisms that have proven effective at boosting participation (auto-enrollment) and contribution rates (auto-escalation). However, the effects of the PPA appear to have played themselves out, and today fewer than half of participants have access to auto-enrollment and a much smaller fraction have auto-escalation.

As a result, 401(k)s are still far short of being a broadly effective retirement savings vehicle.[4] For example:

- About 20 percent of those eligible *still* do not participate in their employer's plan.
- Typical contribution rates fall short of what most workers will need in retirement, and only about 10 percent of participants make the maximum contribution allowed.
- Many individuals make investing missteps, such as putting their money in mutual funds with high fees, which can substantially shrink their assets over time. For example, an additional 100 basis points in fees over a 40-year period reduces final assets by about one fifth.
- About 1.5 percent of assets leaks out of 401(k) plans each year when participants cash out as they change jobs, take hardship withdrawals, withdraw funds after age 59½, or default on loans.

As a result, in 2013, the typical working household approaching retirement with a 401(k) had only $111,000 in combined 401(k) and IRA balances (see Table 2). This amount translates into less than $400 per month, adjusted for inflation, which will not provide a sufficient supplement to Social Security benefits.

And Half of Private Sector Workers Do Not Participate in a Plan

Unfortunately, those workers covered by a 401(k) plan are the lucky ones. Only about half of private sector workers—at any particular time—are participating in any form of employer-sponsored plan, and this share has remained relatively constant over the last 30 years. The lack of universal coverage means that many American workers move in and out of plan participation and a significant percentage will end up with nothing but Social Security. The size of the pension participation gap has recently become controversial.

While the Working Group report got it right, some commentators downplay the problem, citing a Labor Department survey of employers—the *National Compensation Survey* (NCS)—showing that about 80 percent of workers have access to a plan. However, household surveys consistently show that participation rates are in the 40–55 percent range. What accounts for the differences? The answer depends on who, and what, is being measured.

To reconcile the numbers, it helps to compare the NCS employer survey to a Labor Department survey of households—the *Current Population Survey* (CPS) (see Table 3). The NCS shows that, in 2012, 78 percent of employers, public and private,

[4] Munnell (2014).

offered pensions to full-time workers ages 25–64. Excluding public sector workers (who essentially have universal coverage) lowers the figure slightly to 74 percent. Add in part-time workers (who, after all, will still need to save for retirement) and the number drops to 64 percent. Finally, using the percentage of workers who actually *participate* in a plan, rather than those who are *offered* one, reduces the total to 48 percent. This figure compares to 43 percent for the same definition in the CPS, still a difference but only a modest one. In the end, it seems reasonable to conclude that only about half of private sector workers participate in a retirement plan.

THE WORKING GROUP PROPOSALS

The Working Group's report is aimed primarily at reducing this coverage gap and encouraging saving among lower-paid workers. The report discusses four main types of proposals.

First, several proposals would broaden access to potentially low-cost Multiple Employer Plans (MEPs) by getting rid of the requirement that (1) participating employers must share a nexus and (2) one "bad apple" hurts the entire barrel (*i.e.,* a single employer who violates a requirement can disqualify the entire plan). Indeed, MEPs may be a useful vehicle for expanding coverage; making them more available is a positive and appealing step, provided that small employers are protected against unscrupulous actors.

Second, a group of proposals, aimed at small businesses, offer increased financial incentives to start new plans, additional incentives for auto-enrollment, and credits for employer contributions. Other proposals encourage higher matches, less leakage, and the portability of lifetime income. All these proposals would have a positive impact, albeit very small.

Third, a proposal to increase coverage for long-term, part-time employees is a great idea.

Finally, a proposal to enhance the Saver's Credit by increasing eligibility and making the credit refundable is extremely important. We have been doing a lot of work at the State level, and an expanded Saver's Credit could be a very helpful component of the State auto-IRA proposals.

The question is the extent to which these proposals will solve the coverage problem and increase contributions. I fear that their impact will be modest. Making MEPS more accessible does not mean that employers will take advantage of the options. Policymakers have tried to close the coverage gap in the past by introducing streamlined products that can be adopted by small businesses. For example, the SIMPLE plan, which is administered by the employer's financial institution, does not require the employer even to file an annual financial report. These simplification initiatives, however, have clearly not reversed the trend toward declining coverage (see Figure 7).

This outcome is not surprising given that administrative and cost considerations are not the main reasons cited by small businesses for not offering plans (see Figure 8). More important concerns are too few employees, lack of employee interest, unstable business, and other factors. For these reasons, the Working Group's increased financial incentives to set up plans are also likely to have little effect.

The Working Group's proposal to expand the Saver's Credit and make it refundable has the potential for a real impact. To achieve this impact, however, low-wage workers have to make contributions to a retirement account. At this point, relatively few do, because many lack coverage. Expanding coverage, coupled with auto-enrollment, is the only realistic way to achieve this goal. Many States are in the process of setting up their own auto-IRA programs, and the expanded Saver's Credit could be seen as a matching contribution from the government that could encourage workers not to opt out once they are auto-enrolled.

BOLDER STEPS

Given the enormity of the retirement savings crisis, though, we need bolder steps. Within the context of the Working Group report, the two most important changes would be to make the 401(k) system work better and enact auto-IRA legislation at the national level so that each State does not have to set up its own plan.

Make 401(k)s Fully Automatic

The most important policy change would be requiring all 401(k)s to be fully automatic, while continuing to allow workers to opt out if they choose. Plans should automatically enroll *all* of their workers—not just new hires—and the default em-

ployee contribution rate should be set at a meaningful level and then increased until the combined employee contribution and employer match reach 12 percent of wages. The default investment option should be a target-date fund comprised of a portfolio of low-cost index funds.

Separately, the problem of 401(k) leakages needs to be addressed more fully. Recommended changes on this front include tightening the criteria for hardship withdrawals to limit them to unpredictable emergencies; raising the age for penalty-free withdrawals from 59½ to at least 62; and prohibiting cash-outs when switching jobs. These changes would go a long way to making 401(k)s a more robust mechanism for retirement saving. Participants would retain access to their funds in emergencies through loans.

Cover Those Without a Plan

The Working Group recognizes the importance of the coverage gap, but financial incentives alone will not solve the problem. We need to automatically enroll uncovered workers into a retirement savings program. Once employers are required to provide coverage either under a plan that they choose themselves or under a new auto-IRA program, they may become more interested in adopting a MEP, with its low cost and easier accessibility.

As I have noted, many States are setting up their own auto-IRA programs, but it makes much more sense to pass auto-IRA legislation at the national level. Interestingly, anecdotal evidence suggests that opposition towards a national plan among some financial services companies may be softening, as they would prefer a uniform plan to 50 different State plans.

CONCLUSION

The retirement income landscape has been changing in a way that systematically threatens the retirement security of millions of Americans. The Senate Finance Committee could build on the proposals in the Working Group report to make two bold changes—make 401(k)s plans automatic and cover the uncovered through auto-enrolling workers (both full time and career part-time) into a national auto-IRA program. Combine these changes with the expansion of the Saver's Credit and this Committee will have gone a long way towards averting a retirement income crisis.

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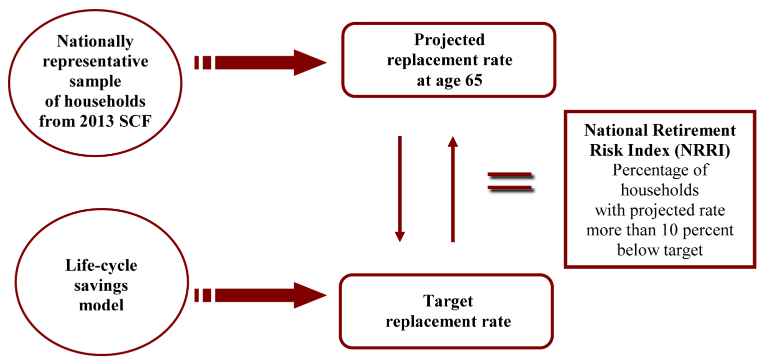
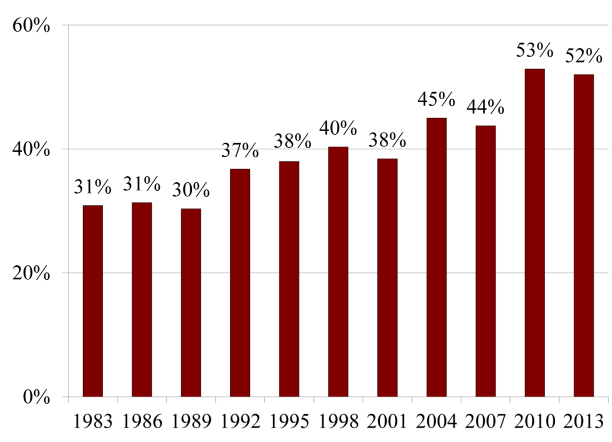
Figure 1. *Overview of the National Retirement Risk Index*



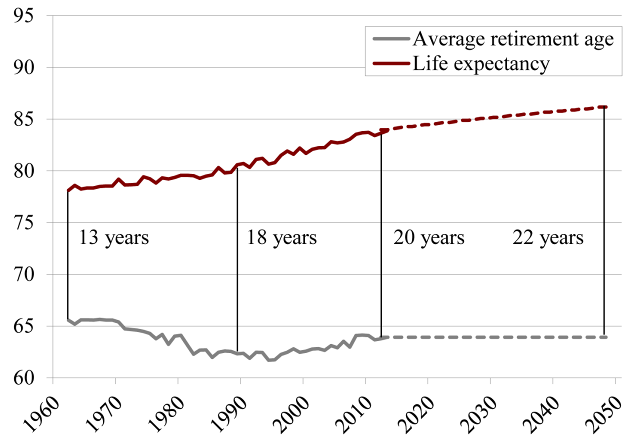
Note: SCF is the *Survey of Consumer Finances*, conducted triennially by the U.S. Board of Governors of the Federal Reserve System.
Source: Author's illustration.

Figure 2. *The National Retirement Risk Index, 1983-2013*



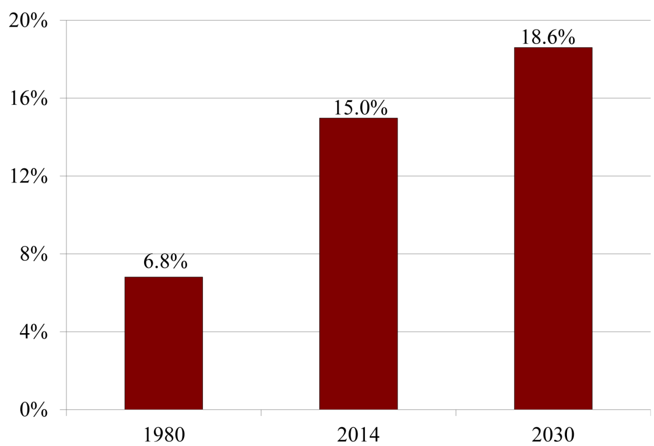
Source: Munnell, Hou, and Webb (2014).

Figure 3. *Average Years in Retirement for Men, 1960-2050*



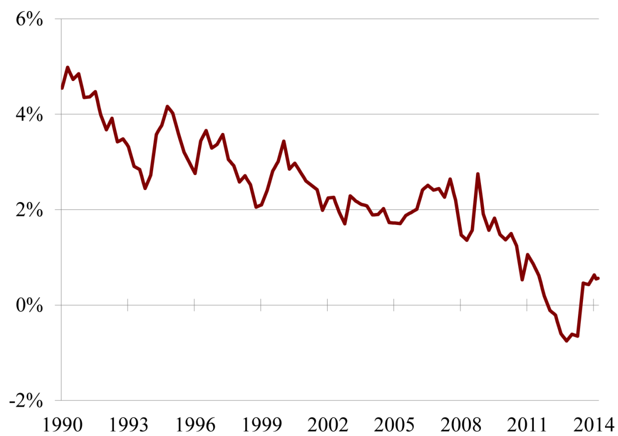
Sources: Author's estimates from U.S. Census Bureau (1962-2012); and U.S. Social Security Administration (2014).

Figure 4. *Medicare Part B Out-of-Pocket Payments as Percentage of Average Social Security Benefits, 1980, 2014, and 2030*



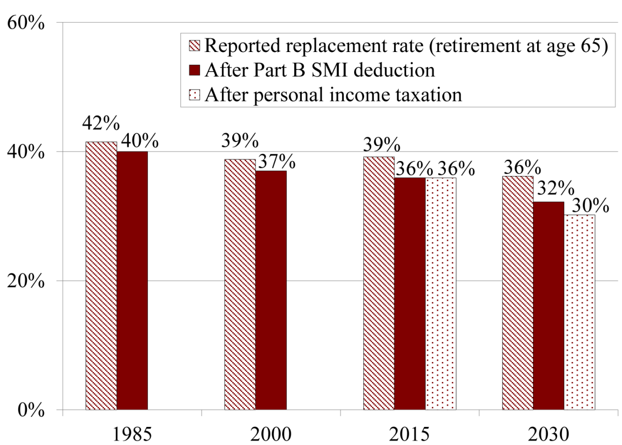
Source: Centers for Medicare & Medicaid Services, Office of the Actuary (2014).

Figure 5. *Real Interest Rate, 1990-2014*



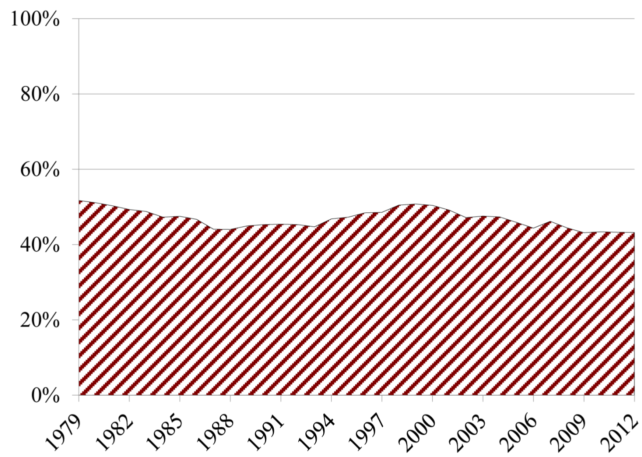
Sources: U.S. Board of Governors of the Federal Reserve System, Selected Interest Rates (2013); Haubrich, Pennacchi, and Ritchken (2011); and unpublished estimates from Richard Kopcke.

Figure 6. *Social Security Replacement Rates for Average Earner Retiring at Age 65, 1985, 2000, 2015, and 2030*



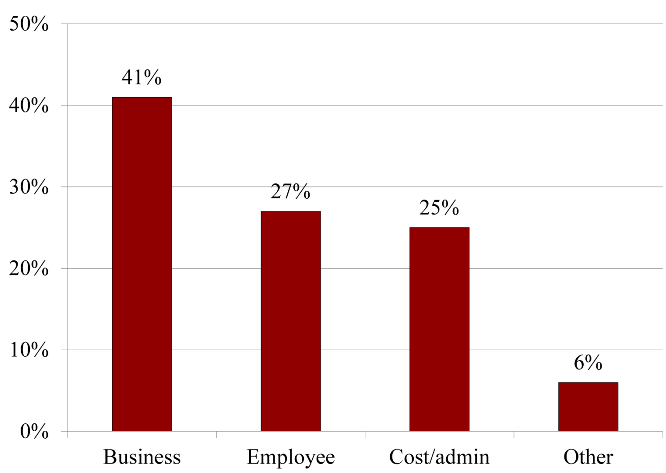
Sources: Author's calculations using unpublished data from Centers for Medicare and Medicaid Services (2014); and U.S. Social Security Administration (2014).

Figure 7. *Percentage of Private Sector Workers Ages 25-64 Participating in an Employer-Sponsored Pension, 1979-2013*



Source: U.S. Census Bureau (1979-2013).

Figure 8. *Most Important Reasons Cited by Small Employers for Not Offering a Plan, 2003*



Source: Employee Benefit Research Institute (2003).

Table 1. Life Expectancy at Age 65 for Men and Women, 1960, 1980, 2000, and 2020

Year	Men	Women
1960	13.2	17.4
1980	14.7	18.8
2000	17.6	20.3
2020	19.7	22.0

Source: U.S. Social Security Administration (2014).

Table 2. 401(k)/IRA Balances for Median Working Household with a 401(k), Age 55–64, by Income Quintile, 2013

Income range (quintiles)	Median 401(k)/IRA balance	Percentage with 401(k)
Less than $39,000	$13,000	22%
$39,000–$60,999	$53,000	48
$61,000-$90,999	$100,000	60
$91,000-$137,999	$132,000	65
$138,000 or more	$452,000	68
Total	$111,000	52

Source: Author's calculations from U.S. Board of Governors of the Federal Reserve System, *Survey of Consumer Finances* (2013).

Table 3. Percentage of Workers (25–64) with Pensions in the CPS and NCS, 2012

Category	CPS	NCS
Employer offers, public and private, full-time	63%	78%
Employer offers, private, full-time	59	74
Employer offers, private, full-time and part-time	52	64
Employee participates, private, full-time and part-time	43	48

Note: CPS is the Current Population Survey. NCS is the National Compensation Survey.
Source: Munnell and Bleckman (2014).

QUESTIONS SUBMITTED FOR THE RECORD TO ALICIA H. MUNNELL, PH.D.

QUESTIONS SUBMITTED BY HON. ORRIN G. HATCH

Question. Dr. Munnell, you mentioned part-time workers in your testimony. The working group identified proposals that would target "long-term" part-time workers, so-called "career part-time" workers who spend 3 or more years in part-time status working for the same employer. As more workers spend lengthy portions of their careers in part-time employment, this seems like an issue that needs to be explored. What are the obstacles to such coverage today, and are they primarily legal or economic in nature?

Answer. No economic rationale exists for excluding "career part-time" workers from retirement plan coverage. I applaud the proposals discussed by the Bipartisan Working Group that would make it impossible to exclude "long-term part-time" employees from coverage on the basis of not having completed a year of service.

Question. As I understand it, the Center for Retirement Research at Boston College, which you direct, receives funding from the Social Security Administration (SSA). Please provide amounts that the Center has received from SSA in each of the past 10 years.

Answer. This information is available through the Social Security Administration.

Question. As a policymaker, I have found it useful to consider various alternative ways to calculate so-called "replacement rates" associated with pensions and Social Security. For a given measure of retirement income, different measures of pre-retirement income (the denominator in the replacement rate calculation) provide different answers and different pieces of information. I do not believe there is a "correct" denominator; what is correct depends partly on the question one is trying to answer. Nonetheless, in an article dated September 2, 2014, posted on the National

Academy of Social Insurance website entitled "Bring Back Social Security Replacement Rates!" you argue that an advocate of consideration of one particular replacement rate measure has pernicious motives. You also argue that in the absence of reports in Social Security Trustees Reports of an alternative replacement rate measure preferred by you, the Social Security actuaries, and perhaps the Organization for Economic Cooperation and Development, "policymakers will have no idea what they are doing to the retirement security of future workers as they consider alternative Social Security provisions." Those to whom you seem to ascribe a pernicious motive are, according to your article, engaged in an "attack on Social Security replacement rates" in "an attempt to provide a rationale for cutting benefits."

As a policymaker, I believe that my colleagues and I do have clear ideas of: how replacement rates can be calculated; how different calculations can answer different questions; and how to perform the various calculations necessary to arrive at replacement rates using various denominators. I also believe that I do, in fact, have clear understandings of implications of alternative Social Security provisions and how they influence retirement security of workers. My question involves recent calculations of Social Security "replacement rates" provided by the non-partisan Congressional Budget Office (December 16, 2015; "CBO's 2015 Long-Term Projections for Social Security: Additional Information"). CBO calculated the rates in a way that I believe you describe as an attack on Social Security replacement rates.

Do you disagree with CBO's use of the denominator it chose for calculating replacement rates—specifically, the average of the last 5 years of "substantial earnings" before age 62?

Do you believe the CBO's reported replacement rates provide a rationale to change Social Security benefits?

Answer. No, I do not disagree with CBO. I think the last 5 years of "substantial earnings" before age 62 is a fine measure of pre-retirement earnings. As you know, the issue was elevated because CBO replacement rates jumped from around 40 percent to around 60 percent with the introduction of this new measure. However, the 60 percent was the result of a programming error, and CBO's corrected numbers are now consistent with the agency's previously reported replacement rates and with those of the Social Security actuaries.

The erroneous CBO replacement rates were being used to argue for benefit reductions. The corrected rates, however, do not provide any rationale to reduce Social Security benefits.

QUESTIONS SUBMITTED BY HON. DEAN HELLER

Question. What is the most important thing lawmakers can do right now to help small businesses offer a workplace savings plan to their employees?

Answer. Left on their own, many small businesses have decided that it is not in their interest to offer a retirement savings plan for their workers. Therefore, the most important change would be to enact a Federal mandate that all businesses without a plan automatically enroll their employees in an IRA. Action at the Federal level is important so that each State does not have to set up its own plan to cover uncovered workers employed by small businesses.

Question. I am deeply concerned with leakage. In my home State, we have felt the pressures of the recession and many of the constituents have had to dip into their retirement funds to make ends meet. In your opinion, what is the single best way we as lawmakers can make it easier for workers to return assets for retirement accounts after they have been withdrawn?

Answer. I agree that leakage is an important issue. It occurs when workers switch jobs, tap their accounts for hardship reasons (as you point out), fail to repay a loan from their account, and take out money at age 59½ when the penalty no longer applies. The best approach may be to close down all avenues of leakage other than loans and then make the repayment of loans as flexible as possible. These changes would ensure that money taken out of the account for emergencies is repaid in an orderly fashion.

Question. I strongly believe that tax reform, done the right way, can improve our fiscal picture. What steps can we as lawmakers take to improve our retirement savings in a fiscally responsible way?

Answer. I think the current tax expenditures for retirement plans are not an effective way to increase retirement saving. Most of the benefits go to people who would have saved for retirement anyway and are of little value to lower income people. It would be more helpful to low-income people to have credits, rather than deductions, and the credit rate could probably be lowered to save tax money. The big point, however, is that tax incentives do not have much effect on savings decisions for anyone. The way to get people to save is to automatically enroll them in a retirement savings plan, with the ability to opt out.

Question. I understand the President is expected to propose an Open-MEP plan in his FY17 budget. I would imagine a significant amount of implementing guidance would be needed. If Open-MEPs were expanded, what role, if any, would the IRS play in this additional guidance?

Answer. I am an economist, not a lawyer. So, unfortunately, I cannot be helpful here.

Question. Like many Nevadans, I am a strong supporter of ways to help our vulnerable populations save long-term for our retirement. What is the single most important thing lawmakers can do right now to help low-income and moderate-income families prepare for retirement?

Answer. Consistent with my earlier response, the most important way to boost retirement savings for low- and moderate-income families would be to enact a Federal mandate that all businesses without a plan automatically enroll their employees in an IRA. These families would also benefit enormously from an expanded Saver's Credit (such as S. 2492), which would make the Credit refundable and essentially serve as a "match" for their IRA contributions.

QUESTION SUBMITTED BY HON. MARIA CANTWELL

Question. In 2015, Washington State became one of the first States in the country to authorize a Small Business Retirement Marketplace, to make it easier and less expensive for small businesses to offer retirement savings options to their employees. Under Washington's program, employers with fewer than 100 employees will be able to voluntarily participate in this marketplace and offer low-cost retirement savings plans, which are portable, to their employees.

Do you believe that this type of marketplace will increase small business participation and make it easier for them to offer a retirement plan for their employees? What is the impact on employees' savings rates when their employer offers a retirement plan compared to those who do not?

Answer. I applaud the initiatives taken at the State level to improve coverage under retirement savings plans. Candidly, though, I am skeptical that the marketplace approach will have much effect. Many small businesses have not introduced plans in the past and, left on their own, are unlikely to do so in the future. Thus, I think the Auto-IRA approach, with a mandate for firms to offer access to a plan, is going to be much more effective than the establishment of marketplaces.

The only place that Americans save is through their employer-provided plans and through paying down the mortgage on their house. People simply do not save for retirement on their own.

QUESTION SUBMITTED BY HON. BENJAMIN L. CARDIN

Question. There are many existing proposals to improve our retirement system. You mention several in your testimony that could increase access to retirement savings as well as increase the amount of savings for those who participate in retirement plans. These are incredibly important issues, and I hope that our committee can take up commonsense, bipartisan proposals to address them.

That being said, while the focus of retirement policy is often rightly on access and accumulation, distribution of retirement benefits over the life of retirees is also very important.

In your view, what steps can we take to encourage lifetime income security? Aside from the suggestions contained in the Savings and Investment Working Group report, are there any other problems, concerns, or reforms that we should consider to address lifetime income and decumulation issues?

Answer. I agree that decumulation is extremely important. When I first looked at this issue, I was worried that everyone would spend down their assets too quickly. But, more recently, I have become concerned that people will instead cling to their assets, depriving themselves of necessities. While people are generally not interested in single premium immediate annuities, the advanced life deferred annuities (ALDAs) (whereby people take about 15 percent of their assets at age 65 to purchase income starting at age 85) seems promising. By assuring retirees that they are not going to run out of money if they live past 85, the ALDA allows them to spend their accumulated assets from age 65 to 85.

QUESTION SUBMITTED BY HON. ROBERT P. CASEY, JR.

Question. In your opinion, what are the most efficient policy options available to make it easier for businesses to help their employees save, or individuals save on their own, and for whom will that most improve retirement and savings outcomes?

Answer. Left on their own, many businesses have decided that it is not in their interest to offer a retirement savings plan for their workers. Therefore, the most important change would be to enact a Federal mandate that all businesses without a plan automatically enroll their employees in an IRA. Action at the Federal level is important so that each State does not have to set up its own plan to cover uncovered workers employed by small businesses.

PREPARED STATEMENT OF HON. RON WYDEN,
A U.S. SENATOR FROM OREGON

Over the last decade or more, policy experts and lawmakers have gathered in rooms like this dissecting this country's growing retirement savings crisis far too many times. That includes a hearing held by this committee about a year and a half ago.

The numbers underlying this crisis are jarring to hear every time. Barely more than half of American workers have access to a retirement savings plan through their employer. A middle-of-the-pack retirement account today has enough saved up to pay a 64 year-old retiree little more than $300 a month. Half of accounts belonging to 55 to 64 year olds have less. And millions of American workers have no pension and nothing saved at all.

Despite those dire statistics, the nonpartisan Joint Committee on Taxation tells us that over the next 5 years, taxpayers will pour more than $1 trillion into subsidies for retirement accounts. It's the second-biggest tax subsidy on the books.

But the Congressional Budget Office says that the benefits are skewed toward people who need help the least. Less than one in five of those dollars goes to households with incomes in the bottom 60 percent of earners.

Minority workers have it even worse. For young workers, or people seeking jobs in restaurants, hotels, or construction, it may be nearly impossible to find an employer who sponsors a retirement plan with a matching contribution. The same could be true in the "gig economy," which is growing every year.

It's clear that working families and the middle class need more opportunities to save—first and foremost at work. Then, the options Americans have for saving need to better reflect the way people work and live in retirement. That means retirement savings built up at work need to be portable and provide a meaningful lifetime income.

The good news is that steps are being taken to create opportunities for saving. Look no further than my home State of Oregon. It's one of three States that has passed what's called an "auto-IRA" law to cover people without employer-based accounts.

Here's the bottom line for Oregon workers—when you get a job, you'll get a retirement account, and you can start saving. It won't be mandatory because workers can opt out, but it's going to relieve a lot of headaches and kick saving into a higher gear.

This was an important step for Oregon to take, because back in 2013, an AARP survey found that one in six middle-aged Oregon workers had less than $5,000 saved. A new report released this month from the Pew Charitable Trusts found that

less than two-thirds of Oregon workers have access to retirement plans through their employers, and barely more than half participated. But Oregon's auto-IRA plan, in my view, represents a sea change. And I hope this trend leads Federal lawmakers to passing the President's national auto-IRA proposal.

Next, the administration has opened up what it calls "My-RA" plans to help workers nationwide get started saving. These smart, new plans are aimed squarely at working Americans of limited means who've been shut out of retirement saving for too long. There aren't any fees to eat into your savings, there are no minimum balance or contribution requirements, and you'll never lose a single penny you put in. It's a great way to start building a nest-egg.

Additionally, there are more proposals in the works that can make a big difference for a lot of workers. Today, I'm introducing a bill to strengthen the saver's tax credit so that it does more for the people who need the most help. At a time when taxpayers are pouring cash into savings incentives that are skewed toward the wealthy, this proposal is one step Congress should take to correct that imbalance.

Furthermore, Senator Hatch and I are working with Senators Brown and Nelson on legislation that expands retirement plans that bring together multiple employers. Our proposal is aimed at getting old rules out of the way, lowering costs, and easing the burden on employers so that this type of retirement plan is available to more workers across the country.

So in addition to big progress with auto-IRAs and My-RAs, these are two important pieces of legislation coming down the pike. Moving forward, I hope to work with the committee on a bipartisan basis to do a lot more to help Americans save for retirement.

Comprehensive tax reform will be a big help. Bills designed to grow wages can make an enormous difference. And the recent turmoil in the markets is a keen reminder of why it's absolutely vital to keep Social Security strong and reject calls for privatization.

Finally I want to say a few words about the multiemployer pension crisis, which absolutely must be solved, and soon. Because of a bad law Congress passed over a year ago—which I opposed—some retirees may face harsh cuts to the pension benefits they've earned. That cannot come to pass, and it must be addressed on a bipartisan basis. In particular, lawmakers need to enact legislation as soon as possible to ensure that many coal miners receive the retiree health and pension benefits they earned over decades of backbreaking work fueling our economy. The situation for mine workers gets worse with every passing day and constitutes a genuine public policy emergency.

I thank the Chairman for agreeing to hold a hearing on this issue, and I look forward to working with him and the other members of the committee on these important issues. I want to thank our witnesses for being here today, and I look forward to our discussion.

Communications

The ERISA Industry Committee (ERIC)

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CONGRESS SHOULD STRONGLY CONSIDER POTENTIAL RAMIFICATIONS THAT CHANGES IN CURRENT LEGISLATION MAY HAVE ON LARGE EMPLOYERS AND THEIR ABILITY TO CONTINUE TO OFFER RETIREMENT PLANS FOR MILLIONS OF AMERICA'S WORKERS

Chairman Hatch, Ranking Member Wyden, and Members of the Committee, thank you for the opportunity to voice the point of view of major employers that directly sponsor voluntary retirement benefit plans for millions of Americans. My name is Annette Guarisco Fildes, and I am President and Chief Executive Officer of The ERISA Industry Committee (ERIC).

ERIC is the only national trade association advocating solely for the employee benefit and compensation interests of the country's largest employers. ERIC supports the ability of its large employer members to tailor retirement, health, and compensation benefits for millions of workers, retirees, and their families. ERIC's members provide comprehensive retirement benefits to millions of active and retired workers and their families. Preserving and enhancing the voluntary employer-provided retirement system and the tax incentives that support it are key policy goals of ERIC and its members.

ERIC believes that financial literacy is the first step in preparing for retirement. Informing America's workers about their retirement options allows them to make better decisions that lead to financial security in retirement. ERIC members are leaders in promoting financial wellness programs that have increased employee engagement and improved financial health. ERIC members have undertaken programs that educate their employees on a variety of financial topics, including preretirement planning, cash and debt management, tax planning, funding higher education, and investing.

ERIC believes that as proposals aimed at increasing the participation of small employers in the retirement system are developed, this Committee and Congress should strongly consider potential ramifications that changes in current law may have on large employers and their ability to continue to offer voluntary employer-sponsored retirement plans for millions of American workers. I would like to highlight key aspects of the current employer-sponsored retirement system that support the ability of large employers to continue providing retirement benefits to millions of workers.

ERIC and its members believe the following policy goals are critical to the continuation of the employer-sponsored retirement system, and recommend that the Committee consider the following with respect to retirement plans:

(1) Preservation of the voluntary nature of employer-sponsored retirement plans.

Employer-sponsored retirement plans are critical to the continuation of the employer-sponsored retirement system. The voluntary nature of the retirement plan

system works well as a result of the flexibility provided to employers and their workers.

Employers voluntarily establish retirement plans to compete for and retain quality workers and to ensure workers are able to retire with adequate retirement savings. The voluntary nature of the private-sector retirement system is vital to its success. No two employers are identical; some employ thousands of workers, while others employ only a few. Employers are engaged in different industries, located in different geographical regions; some operate in the global market, while others operate only in their local community. A "one-size-fits-all" approach to rules and regulations often will not address the challenges of every company that wants to offer retirement benefits to their workers.

Flexibility is critical in retirement plans. It allows employers to design plans that work effectively and efficiently based on the needs of their diverse workforces. Rules that are too onerous or overly restrictive can chill an employer's commitment to offer and a participant's interest to participate in an employer-sponsored plan.

The voluntary nature of the current employer-sponsored private retirement system and the flexibility employers have in establishing and maintaining retirement plans for their workers is vital to America's private retirement system. Congress should ensure the current private retirement system remains voluntary and flexible to encourage continued, and new, employer participation.

(2) Preservation of current tax incentives for retirement benefits.

Removing the current tax incentives for retirement plans will discourage plan establishment and maintenance and reduce the participation of employees contributing to their retirement savings.

Unlike tax expenditures where tax is completely avoided (*i.e.,* deductions), taxes on retirement plan contributions are generally merely *deferred* until the participant receives a distribution of the funds, which is typically during retirement. In the unusual event a participant takes a pre-retirement distribution, there is an additional tax penalty, absent a qualifying case of hardship, which results in additional money for the government. Tax revenue is not completely lost when workers contribute to their retirement plans—it is merely delayed.

When measuring the cost of tax deferrals in retirement plans, such as 401(k) plans, the calculations performed by the Joint Committee on Taxation (JCT) and the Treasury Department do not consider that there is only a deferral of taxation. Workers generally withdraw money from these plans only in retirement, the majority of the taxes paid show up outside the 10-year time frame used for revenue estimates. As a result, the majority of the costs for deferrals is "scored" as lost revenue. The approach used by the JCT and the Treasury Department significantly exaggerates the actual cost to the government with respect to the tax incentives for retirement plans and ignores the real long-term value of the plans to the country and working Americans. Intricacies in the federal budget rules unfortunately result in retirement plan tax deferrals being counted as a revenue loss without taking into account the corresponding deferred gain.

Continuing to provide tax incentives encourages both employer and worker participation in America's retirement system. Because taxes are merely deferred, not excluded, Congress should ensure that employer-sponsored retirement plans continue to receive the long-standing protections on which employers and workers rely.

(3) Ensuring appropriate deferral and contribution limits that reflect current inflation rates and economic circumstances.

Workers need flexibility to be able to save more when they are able and less when they are under financial constraints. For example, an individual may be able to save more when they are younger or once their children become adults, but have less money to contribute when paying for their children's college education or caring for their elderly parents.

Under the current system, employees are able to make elective deferrals up to $18,000 annually. Congress recognized the need for older workers to save more as they are nearing retirement. As a result, workers age 50 and older can currently save up to $24,000 annually. Policymakers have acknowledged that the "savings cycle" can be different depending on an individual's unique circumstances.

We encourage the Committee to reconsider the current deferral limits, which have not kept up with inflation, at a minimum. The limit on contributions made on an individual's behalf to a defined contribution plan was set at $25,000 (and indexed

to inflation) when ERISA was enacted in 1974.[1] By 1982, the limit had increased to $45,475.[2] However, the Tax Equity and Fiscal Responsibility Act of 1982 reduced the limit to $30,000 and postponed indexation until after 1985. Indexation was again deferred until after 1987 by the Deficit Reduction Act of 1984. Then, in 1986, the contribution limit was frozen at $30,000 through 2000 as a result of the Tax Reform Act. Since 2001 the limit has gradually increased to $53,000,[3] not much above the 1982 limit of $45,475, and far below the amount that the 1974 limit of $25,000 would represent in 2016 dollars—$133,673.[4]

Proposals that would limit the amount of retirement plan contributions, reduce the current contribution deferrals, or limit the value of the retirement benefits would undermine the success of the current employer-sponsored retirement system by discouraging employers from establishing and maintaining plans and causing some participants to decrease their contributions. The result would be reduced savings balances at retirement by 6 to 22 percent for workers currently age 26–35 with the greatest reductions for those in the lowest-income quartile[5]—the demographic that Congress seeks to encourage to save more.

In the 1980s, we saw the significant negative consequences when a well-intentioned Congress set out to limit retirement contributions. When Congress complicated the eligibility requirements for individual retirement accounts (IRAs), deductible contributions declined from $37.8 billion in 1986 to only $14.1 billion in 1987 and continued to steadily decline thereafter.[6] Workers have shown that they will respond to increased complexity in retirement plans by saving less.

It is critical that Congress recognize the value of the current system that reflects typical lifetime savings habits and consider increasing the elective deferral limit. We urge the Committee to continue to support and expand the ability of individuals to save through their workplace retirement plans by continuing COLA increases to deferral limits and reviewing the adequacy of the 402(g) limits in the Internal Revenue Code. Any changes to retirement savings incentives must focus on policy that will result in better long-term retirement outcomes for Americans, rather than on raising federal revenue.

(4) Ensuring PBGC premiums are increased only as needed for the sole purpose of maintaining the single employer trust fund for the benefit of workers and retirees.

The Pension Benefit Guaranty Corporation (PBGC) plays an important role in protecting the retirement benefits of millions of America's workers. PBGC carries out its mission by ensuring that employer-sponsored defined benefit pension plans are adequately funded, which it does, in part, by collecting insurance premiums from employers sponsoring such plans. The PBGC is not funded by general tax revenues. Accordingly, PBGC should not be used as a vehicle for funding the general budget. Premiums paid to PBGC by employers should be increased as needed solely to achieve their intended purpose—to ensure adequate funds are available for pension plan liabilities in the event an employer sponsoring a pension plan is forced into bankruptcy.

Money spent on PBGC premiums takes away from funds that employers can use for worker benefits, business expansion, job creation, and other contributions to economic growth. When Congress increases PBGC premiums absent necessity or improperly allocates premiums, it increases economic uncertainty and job loss while chilling investments and economic growth.

Despite Congress's mandate that PBGC is to encourage employers to continue and maintain voluntary private pension plans, plan sponsors have been replacing de-

[1] 26 U.S.C. 415(c) 1974.

[2] Investment Company Institute, *401(k) Plans: A 25-Year Retrospective,* 12 RESEARCH PERSPECTIVE (Nov. 2006), *available at https://www.ici.org/pdf/per12-02.pdf.*

[3] 26 U.S.C. 415(b) (1974). *See* EMP. BENEFIT RESEARCH INST., *EBRI's Fundamentals of Employee Benefit Programs 50* (2009), *available at https://www.ebri.org/pdf/publications/books/fundamentals/2009/05_Ret-Plans_RETIREMENT_Funds_2009_EBRI.pdf.*

[4] *Inflation Calculator with U.S. CPI Data, http://www.calculator.net/inflation-calculator.html?cstartingamount1=25000&cinyear1=1974&coutyear1=2016&calctype=1&x=57&y=8* (last visited Feb. 2, 2016).

[5] Jack VanDerhei, *Modifying the Federal Tax Treatment of 401(k) Plan Contributions: Projected Impact on Participant Account Balances,* 33 EMP. BENEFIT RESEARCH INST. NOTES (Mar. 2012), *available at https://www.ebri.org/pdf/notespdf/EBRI_Notes_03_Mar-12.Ktaxes-PThlthCvg1.pdf.*

[6] Sarah Holden, et al., Investment Company Institute, *The Individual Retirement Account at Age 30: A Retrospective,* 11 RESEARCH PERSPECTIVE (Feb. 2005), *available at https://www.ici.org/pdf/per11-01.pdf.*

fined benefit pension plans with defined contribution plans to avoid increased premiums. PBGC premiums already account for more than 13 percent of total defined benefit plan expenses. Sponsors paid premiums on 2.5 million fewer participants in 2014 than in 2011 as a result of leaving the defined benefit system to alleviate premium burdens.

ERISA requires that PBGC premiums be paid directly to the PBGC for the purpose of crediting funds used to pay benefits to plan participants. The Treasury Department's practice of counting increased PBGC premiums as general revenue for the budget exhibits poor governance and weakens the nation's retirement system and ultimately harms employees and retirees. PBGC premiums should be increased only as needed to ensure retirement benefits are adequately protected. ERIC also encourages the Committee to consider advancing legislation that devotes PBGC premiums solely to the PBGC program, taking them "off-budget" so that they can no longer be used as revenue for unrelated programs.

(5) Maintaining the IRS determination letter program for large complex retirement plans.

The IRS's decision to eliminate determination letters for individually-designed retirement plans disproportionately affects large employers and ultimately may diminish retirement benefits for America's workers. Larger employers need flexibility to make routine changes to their retirement plans to conform with new laws, reflect mergers, acquisitions, or spin-offs, or to implement new and innovative changes that are in the participants' best interests.

The IRS answer is for plan sponsors to use prototype plans. Large employers have complex plan designs and generally cannot use pre-approved documents due to the inherent limitations of the format. Their use of the IRS's model amendments requires substantial revisions and is simply unworkable. According to Employee Benefit Research Institute (EBRI) tabulations of 2012 Form 5500 filings, 98.4 percent of pension plans with at least 5,000 participants do not use prototype plans. Eliminating the IRS determination letter program adversely affects the attractiveness of retirement plans to large employers (and even more so for large employers who continue to sponsor defined benefit retirement plans), including ERIC's members, and results in participants and beneficiaries questioning their own tax positions (as, for example, in their ability to make a rollover to another qualified plan).

As a measure of prudence, we believe the determination letter program should be maintained for large complex retirement plans and we ask for the Committee's support to encourage the IRS to retain the program for plan sponsors with at least 15,000 participants or $500 million in plan assets.

(6) Facilitating the electronic distribution of retirement plan information.

ERIC supports modernizing the communication of retirement plan information from large employers to their plan participants and beneficiaries. Today the Labor Department requires that participant information, such as summary plan descriptions, summaries of material modifications, quarterly pension benefit statements, annual funding notices, and a variety of other notices, be given in paper format. While the Department provides a current safe harbor for electronic disclosure under specific circumstances,[7] the safe harbor's significant restrictions render electronic disclosure impractical or, in many cases, impossible.

Electronic distribution of retirement plan information reflects today's communication norms. America's workers increasingly prefer to receive communications electronically, including information concerning their retirement plans. Electronic distribution allows participants to easily store plan information in a single convenient location available for access anytime and anywhere. Electronic communications have become more reliable than mailing paper documents, which may be misdelivered or otherwise lost in the mail. Electronic distribution is also more cost effective, as it will significantly reduce shipping and paper costs. Participants who may not have access to the Internet or prefer a paper copy should be allowed to elect to continue to receive plan information in paper form, but the default should be electronic. We ask the Committee to support legislation to allow employers to efficiently and effectively communicate plan information with plan participants electronically, as long as participants are able to choose a paper alternative.

In conclusion, the employer-sponsored retirement system provides the bulwark of retirement security for working and retired Americans. As a result, it is important

[7] *See* 29 CFR 2520.104b–1(c).

that Congress protect the value provided by the current retirement plan system and avoid changes that could result in unintended adverse consequences to the country and its workers and retirees. We urge the Committee to strongly consider key aspects of the retirement system that allow large employers to provide robust retirement benefits to millions of American workers when implementing changes to the current system for small employers.

THE ESOP ASSOCIATION

Statement for the Record for

Full Committee Hearing

"Helping Americans Prepare for Retirement: Increasing Access, Participation, and Coverage in Retirement Savings Plans"

January 28, 2016

The following statement is submitted by The ESOP Association, located at 1200 18th Street, NW, #1125, Washington, DC 20036, phone 202–293–2971. The person who drafted the following statement is J. Michael Keeling, President, email michael@esopassociation.org.

Before setting forth the evidence why employee stock ownership plans, referred to as ESOPs, should be promoted and encouraged as good retirement savings plans, it is appropriate to set forth what an ESOP is, and its history, especially the specific role played by the Senate Finance Committee for the past 41 years in the creation of laws promoting the creation and operation of employee stock ownership via the ESOP model.

What Is an ESOP?

Unique among ERISA plans, an ESOP, by law, *must be* primarily invested in the highest class of stock of the plan sponsor and the stock may be acquired with borrowed funds. In practical terms, the plan sponsor may take on "debt" to acquire shares of the sponsor, and not be engaged in a prohibited transaction if the shares are acquired by the ESOP trust at a price no greater than the fair market value.

Brief History of ESOPs

The ESOP model of employee ownership actually has its roots in a compensation practice from the 19th Century. (A recent book, "The Citizen's Share," Blasi, Freeman, and Kruse, Yale Press, wrote a very convincing case, pages 1–56, that our founding fathers, such as Washington, Jefferson, Adams, Hamilton, et al., believed in broad ownership of productive assets as being essential to the survival of a democracy. President Lincoln's views, as evidenced by the Homestead Act, were also in sync with our founding fathers' views.)

As the U.S. economy moved into the industrial age, corporations with nationwide reach, and large numbers of employees emerged—Procter and Gamble, Montgomery Ward, and others. Leaders of these companies realized that some employees would work for many years, reach an age requiring retirement, and retire with no income. There was no 19th Century safety net for retirees, and leaders of a number of national firms decided to set aside company stock for the employees to have when they retired, and to "cash in."

After World War I, and the ratification of the 161 Amendment to the Constitution authorizing a national income tax, Congress recognized that taxing income was not so simple, and that many issues had arisen because the basic definition that income is anything of value received by an individual, and the general rule that an income tax should tax anything of value.

In response to questions of what income should be taxed, Congress developed the very first true income tax code, the Code of 1921.

In developing the Code, those firms that were setting aside stock for their retiring employees came to the House Committee on Ways and Means and asked—"Is the stock set aside for an employee's retirement taxable when set aside, and is the value of the stock an employer's compensation cost?"

The Ways and Means Committee decided no, it was not current income to the employee, but would be taxed when the employee realized the previously deferred in-

come; and yes, the set aside was compensation, and thus a cost of business for the employer and thus deductible for income tax purposes.

Thus, the first deferred compensation plan recognized by Congress was the "stock bonus plan," the forerunner of today's ESOP.

Fast forward to post War World II and owners of privately held businesses began to consider how to "exit" their businesses and "cash" in their non-tradable stock in the company they started and which had become successful because of the hard work of the company employees. While somewhat lost in history due to the fact that until the mid-1970s private letter rulings were not public documents, an owner in Alaska, followed by others, obtained permission from the IRS, in a non-public letter ruling, that the company could "buy" his stock with borrowed money, have the stock placed in the company's stock bonus plan, and have the stock allocated to the employees as the debt was paid off.

A true visionary in San Francisco, California, Dr. Louis O. Kelso, developed a comprehensive economic philosophy in using such a method for funding stock bonus plans to expand ownership in a capitalistic society and to facilitate capitalization of for-profit businesses. He and his law firm colleagues led the way in expanding the use of this method blessed by the letter rulings, and many correctly note that the first "ESOP" was the sale by exiting shareholders of the *Monterrey Press* north of San Francisco in 1957 to an ESOP.

By the mid-1950s, many, both conservative and liberals, were seeing abuses in the area of pensions, or tax qualified deferred compensation plans, which the tax laws sanctioned and encouraged. Evidence was overwhelming that some pension funds were investing in organized crime activities. Then there was the collapse of major U.S. employers, leaving employees with no retirement income as promised. As a result, a drive in Congress to "reform" the tax and labor laws governing tax qualified deferred compensation plans, or "retirement savings plans," led to the enactment of ERISA in 1974.

During Congressional work on these "tax qualified deferred compensation plans," a major influence on tax policy of that era, Senator Russell B. Long, long time chair of the Senate Committee on Finance became a champion of the economic philosophy of Dr. Kelso, and made sure the new ERISA law sanctioned ESOPs.

His support for the ESOP model grew stronger with each passing year, and his leadership led to major enactment of tax laws promoting the creation and operation of ESOPs. The bulk of these laws passed in 1984, in legislation referred to as DEFRA, and the perfection of those laws were in the Tax Reform Act of 1986.

Many of these laws of the 1980s remain in the Code, and were evidenced and endorsed repeatedly by the Finance Committee members in hearings, and tax law legislation of the late 1980s through the late 1990s, even after Senator Long retired in 1987.

To be noted, a major partner with Senator Long promoting ESOPs in the 1980s through 1988, was former President Ronald Reagan, who often spoke of his view that widespread ownership of productive assets was the core of maintaining equitable wealth ratios in a capitalistic society.

And, after Senator Long retired, his successor in the Senate, former Senator John Breaux, led the expansion of ESOP law in the 1996–1997 tax bills permitting S corporations to sponsor ESOPs. Since Senator Breaux's work to expand ESOPs, the number of 100 percent ESOPs that are S corporations has exploded. (There are out of the estimated 10,000 ESOP companies, an estimated 3,000 are 100 percent ESOP.)

In sum, the review the Finance Committee is doing is part and parcel of a long, supportive policy of the Finance Committee's developing laws to have average pay employees, or workers if you will, be owners as being good for the employees, good for their employer, and good for the well-being of our economy and democracy.

Recent Finance Committee Positions on ESOPs

But when reviewing the record of the Senate Finance Committee on ESOPs, it is not all ancient history, involving men and women of the Senate from years ago.

For example, in the first quarter of 2015, Chair Hatch, with a goal of having members of the Committee, in a bi-partisan effort, established "tasks forces" to review major areas of the current tax code, with an eye towards reform. One task force was the "Tax Reform Group on Savings and Investments," which as part of

its review reviewed current law with regard to encouraging the creation and operation of ESOPs. The co-chairs of the S&I Task Force were Senators Crapo and Brown, again bi-partisan leadership.

Page 13 of the memo to the Chair and full Committee of its recommendations was a recommendation that S. 1212, be included in any tax reform bill's provisions on retirement savings and investments.

(As an aside, currently S. 1212, introduced by Finance Committee member Senator Cardin on May 6, 2015, is co-sponsored by 28 other members of the Senate, broken down by 14 Republicans, 13 Democrats, and 2 independents, including 8 members of the Finance Committee. Fifteen other Senators, 5 on the Finance Committee, co-sponsored the same bill in the 113th Congress.)

Page 13 of the S&I Task Force endorsed S. 1212 because of the track record of ESOPs providing retirement security for employee-owners of both small and large businesses.

To be noted that early in the second quarter of the past year, the Senate Committee on Small Business suggested that the provisions of S. 1212 be included in any tax reform bill developed by the Committee on Finance. (Copy of S. 1212 Attachment 1)

The question is **WHY?** Why has a bi-partisan group of women and men serving in the Senate renewed evidence of a mainstream view set forth by the Finance Committee since 1975 that the expansion of employee stock ownership via the ESOP model would be good public policy?

Just to include in this statement for the record some of the same evidence motivating the recommendation from last, and some reinforcing evidence.

1. Since the 2002 prestigious General Social Survey up to the recently released 2014 GSS, evidences clearly that companies with employee stock ownership are much more likely to have layoff rates that are significantly less than conventionally owned companies—3 percent in 2002 for companies with employee ownership, 9.2 percent conventionally owned; 2006, 2.3 percent versus 8.5 percent; 2010, 2.6 percent versus 12.3 percent; and 2014, 1.3 percent versus 9.5 percent. Most impressive are the 2010 numbers, reflecting layoffs during the Great Recession. (Note that further data crunching by the National Center for Employee Ownership indicated that the fact these companies with employee stock ownership had fewer layoffs generated $14 billion dollars due to employees paying income, Social Security, and Medicare taxes, and not taking Unemployment Compensation or Food Stamps, seven times more than the general revenue estimates for the "tax expenditures" of special ESOP tax rules.)
2. A study of 1,100 ESOP companies in the late 1990s, compared to counterparts in the same industry, by Rutgers Professors Dr. Blasi, and Kruse, evidenced the ESOP companies had better sales, more employment, and were by a rate of 16 percent greater than their competitors over an 11 year period remained independent.
3. Highly valued as a one source of history and data about employee stock ownership, and the ESOP model in particular, is the well selling book "The Citizen's Share," by Drs. Blasi and Kruse of Rutgers, and Dr. Freeman of Harvard. The easy to read volume contains reference to nearly all of the research over the past 30 years with regard to the performance of ESOPs, both as a wealth creation, retirement savings, and as a jobs policy.

Attachment 2 is a fuller summary of research and its data of the track record of ESOP companies, and their reward of average pay employees.

In sum, Chair Hatch and members of the Committee on Finance, there is ample data, and real world experience to continue the push by the Committee to increase employee stock ownership. Bottom line, ESOPs are more productive, more sustainable, with jobs controlled by U.S. interests, providing retirement savings for average pay employees than other savings plans, and making our nation more competitive.

Attachment 1

Summary of S. 1212 "Promotion and Expansion of Private Employee Ownership Act of 2015" Introduced May 6, 2015

S. 1212 will:

- Permit owners of S stock to sell the stock to an ESOP and defer the capital gains tax on his/her gain if the proceeds are reinvested in the equities of U.S. operating corporations as owners of C corporations stock have done under IRC 1042 since 1984;
- Establish an office in the Department of Treasury to provide technical assistance to S corporations with ESOPs; and
- Provide that a small business, S or C, eligible for one of the many programs provided by the Small Business Administration referred to as 8A preference programs to remain eligible for SBA 8A programs if and when the company becomes owned 50 percent or more by an ESOP, and the workforce remains the same or nearly the same as before the establishment of the 50 percent ownership by employees through the ESOP.

General Explanation Why S. 1212 Should Become Law

1. There is ample macro-data evidencing that the benefits our ESOP provides to [name of company] is also the case in the vast majority of privately held ESOP companies in America.
2. S. 1212 is a modest proposal that will not cost any significant tax revenues, and will build even larger account balances for retired employee owners, who will pay more taxes on their ESOP distributions than the targeted tax expenditure for ESOPs in H.R. 4837. For example, more ESOPs will be created, certain existing ESOP small businesses will qualify for SBA loans, and all S ESOP private companies can access Treasury experts on the complex rules governing S ESOPs.
3. In short S. 1212 will address the growing concerns of individual access to ownership, equitable distribution of our nation's capitalism, in companies that are more productive, more profitable, and more sustainable providing locally controlled jobs.

Attachment 2

Employee Owners Impact Corporate Performance Positively; Overwhelming Evidence ESOP Companies More Productive, More Profitable, and More Sustainable, Providing Locally Controlled Jobs

- During the Great Recession, employee stock owned companies laid off employees at a rate of less than 3 percent, whereas conventionally owned companies laid off at a rate greater than 12 percent. (Data source: 2010 General Social Survey.)
- Because employees of ESOP companies were four times more likely to retain jobs during the Great Recession, Federal government recognized savings of over $14 billion in 2010 compared to tax. payments foregone by laid off employees of conventionally owned companies; in other words for every $1 in tax expenditures to promote employee stock ownership, the Federal government collected $13 in taxes. (Data Source: 2010 General Social Survey analyzed by National Center for Employee Ownership.)
- A survey of 1,400 ESOP companies in 2010 evidenced the average age of the companies' ESOPs were 15 years, and the average account balances for employees were nearly $200,000, much higher than data reported for average 401(k) account balances. (The ESOP Company Survey, 2010, of The ESOP Association's Corporate members.)
- According to 2012 General Social Survey, 13 percent of employees of employee stock-owned companies were thinking of seeking employment elsewhere, whereas 24 percent of the employees of conventionally owned companies were considering leaving their current job.

- In the summer of 2014, the Employee Ownership Foundation released results from the 23rd Annual Economic Performance Survey (EPS) of ESOP companies. Since the Employee Ownership Foundation's annual economic survey began 23 years ago, a very high percentage, 93 percent of survey respondents, have consistently agreed that creating employee ownership through an ESOP was "a good business decision that has helped the company." It should be noted that this figure has been over 85 percent for the last 14 years the survey has been conducted. In addition, 76 percent of respondents indicated the ESOP positively affected the overall productivity of the employee owners. In terms of revenue and profitability—70 percent of respondents noted that revenue increased and 64 percent of respondents reported that profitability increased. In terms of stock value, the majority of respondents, 80 percent, stated the company's stock value increased as determined by outside independent valuations; 18 percent of the respondents reported a decline in share value; 2 percent reported no change. The survey also asked respondents what year the ESOP was established. Among those responding to this survey, the average age of the ESOP was 16 years with the average year for establishment being 1998.
- More than half of the ESOP companies have two retirement savings plan (primarily a 401(k)), whereas more than half of all companies have *no* retirement income savings plan. (Analysis of forms 5500, and Bureau of Labor Statistics by the National Center for Employee Ownership, funded by the Employee Ownership Foundation.)
- The average ESOP company (less than 200 employees) has sales $9 million more per year than its non-employee owned comparable competition. (June 2008 Dissertation, Dr. Brent Kramer, CUNY.)
- A study of 1,100 ESOP companies over eleven years compared to 1,100 comparable conventional owned companies evidenced the 1,100 ESOP companies had better sales, more employment, and were more likely over the period to remain independent businesses by 16 percent. (Most detailed study of ESOP companies by Dr. Joseph Blasi, and Dr. Douglas Kruse, tenured professors, Rutgers University School of Labor and Management, 1999.)

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Washington, DC 20005

United States Senate Committee on Finance

Hearing: "Helping Americans Prepare for Retirement: Increasing Access, Participation, and Coverage in Retirement Savings Plans"

Testimony of Catherine Weatherford
President and CEO. Insured Retirement Institute

January 28, 2016

Chairman Hatch, Ranking Member Wyden, and Members of the Full Committee, my name is Cathy Weatherford, and I am the President and CEO of the Insured Retirement Institute (IRI). On behalf of IRI, I am pleased to provide IRI's perspective on your hearing titled "Helping Americans Save for Retirement: Increasing Access, Participation, and Coverage in Retirement Savings Plans." I commend you for holding this hearing, and I value the opportunity to provide testimony.

IRI's member companies also appreciate the Tax Reform Working Group on Savings and Investment for issuing key goals for policy makers to pursue. Committee Members and staff were dedicated and committed to a process that allowed stakeholders such as IRI to contribute ideas that led to the development of the report's recommendations.

About the Insured Retirement Institute

As you may know, I have over 30 years of regulatory experience, including having spent more than half of that time as an elected Insurance Commissioner and Insurance Department staff in the State of Oklahoma. Prior to joining IRI, I served as

the CEO of the National Association of Insurance Commissioners for 12 years, where I worked with over 50 state insurance commissioners to craft important consumer protections, including critical measures aimed at safeguarding our nation's seniors. I joined IRI because my life's work is perfectly aligned with IRI's mission.

IRI is the leading association for the retirement income industry. As a not-for-profit organization, IRI provides an objective forum for communication and education, and advocates for the retirement strategies Americans need to help achieve a secure and dignified retirement. IRI also proudly leads a national consumer coalition of more than 30 organizations that work to promote retirement planning.

IRI is the only national trade association that represents the entire supply chain for the retirement income industry. We have more than 500 member companies, including major insurance companies such as TIAA–CREF, Prudential and MetLife, banks such as Wells Fargo and PNC asset management companies such as Franklin Templeton Investments and T. Rowe Price, and broker-dealers such as Morgan Stanley, Raymond James, Edward Jones, and LPL Financial, who have affiliated financial advisors in communities across America. IRI member companies represent more than 95 percent of annuity assets, and include the top 10 distributors ranked by assets under management. We offer education, research and advocacy resources to more than 150,000 financial advisors and more than 10,000 home office professionals affiliated with our member companies.

Our members are represented by hundreds of thousands of registered financial advisors across the country, and therefore, we bring a perspective from Main Street America to Congress. After my many conversations with these financial advisors, I have developed a deep level of appreciation for the longstanding relationships they have with their clients and friends, often lasting for 10, 20, or even 40 years. Our financial advisors consider these relationships to be a sacred trust and, as such, they are intensely committed to helping their clients reach their retirement income objectives, which involves a series of the most significant financial decisions a person ever makes over a very long lifetime.

America's Retirement Income Challenge: The Need for Retirement Income Products, Lifetime Income Options and Professional Financial Help

Americans today are at risk of outliving their assets. This longevity risk has never been greater. The shift from defined benefit to defined contribution plans, longer life spans, and the rising costs of health care are among the challenges that will put significant financial pressures on the shoulders of individual consumers, in particular middle-income Americans. These challenges simply did not exist in earlier generations.

At the peak in 1985, over 114,000 private-sector defined benefit plans were in place,[1] but by 2015 less than 24,000 of these defined benefit plans remained.[2] Only 8 percent of private-sector workers had access to a defined benefit plan in 2015.[3]

Individuals are living longer than those of earlier generations. The population of older Americans continues to increase at a faster rate than the overall population. For example, between 2000 and 2010, the number of Americans aged 85 to 94 grew by 29.9 percent; by comparison the entire U.S. population increased by 9.7 percent during that timeframe.[4] Moreover, according to the Society of Actuaries, a married couple age 65 has more than a 65 percent chance of one or both living to age 90, and a 35 percent chance of one spouse living to age 95.[5]

As a result of these trends, today more than 30 million Baby Boomers are "at risk" of having inadequate retirement income, that is not having sufficient guaranteed lifetime income.[6] Just as concerning, nearly half (45 percent) of Generation Xers (ages 36–45) are "at risk" of having inadequate retirement income.[7] Alarmingly, only 40 percent of Americans 30 to 49 years of age have tried to determine how

[1] Pension Benefit Guaranty Corporation. *Trends in Defined Benefit Pension Plans.*
[2] Pension Benefit Guaranty Corporation. *Pension Benefit Guaranty Corporation Annual Report 2015.*
[3] Bureau of Labor Statistics. *National Compensation Survey: Employee Benefits in the United States, March 2015.*
[4] United States Census Bureau. *The Older Population 2010.*
[5] Society of Actuaries. *SOA 2012 Individual Annuitant Mortality Tables.*
[6] Employee Benefit Research Institute. *EBRI Notes: Retirement Income Adequacy for Boomers and Gen-Xers: Evidence from the 2012 EBRI Retirement Security Projection Model.*
[7] *Id.*

much they need to save by the time they retire.[8] Meanwhile, nearly one-third of Baby Boomers cite having adequate retirement assets as a top concern, while over three-quarters said they will work for income in retirement, meaning they actually will not be retired.[9]

This reality underscores the critical importance of a regulatory environment that provides consumers access to products that meet their need to protect against longevity risk, as well as one that increases access to tax-deferred retirement savings. It also emphasizes the need for the advancement of both common sense retirement security policies and initiatives to promote consumer education and choice.

Guaranteeing Lifetime Income With Insured Retirement Products

Annuities are the only financial instruments available today, other than Social Security and pensions, that can guarantee a lifetime stream of income during retirement, and only insurance companies and their distribution partners can provide these products. With the proper use of annuities and other guaranteed lifetime income products, retirees can be assured they will not outlive their assets. Boomers who own insured retirement products, including all types of annuities, have higher confidence in their overall retirement expectations, with 9 out of 10 believing they are doing a good job preparing financially for retirement.[10] Compared to non-owners, Baby Boomers who own annuities—by more than a two-to-one ratio—are likely to be among those who are most confident in living comfortably throughout their retirement years.[11] Baby Boomer annuity owners also are more likely to engage in positive retirement planning behaviors than Baby Boomer non-annuity owners, with 68 percent having calculated a retirement goal and 63 percent having consulted with a financial advisor.[12]

Proposals Related to Retirement Savings and Lifetime Income

The Insured Retirement Institute recently released its 2016 legislative agenda. The principle of protecting and expanding access to American retirement savers is at its foundation. Our agenda identifies policy solutions to expand access to workplace retirement plans that help Americans save and prepare for retirement; to increase access to lifetime income options that help Americans ensure their savings will not be outlived; and to improve access to education and information that American savers need to make better and more-informed decisions regarding their finances. Below are a number of our priorities that we hope the Senate Finance Committee will pursue:

Provide Multiple Employer Plans (MEPs) With Lifetime Income Options

All small employers should be able to join multiple employer plans, or MEPs, which will result in more workers having access to retirement plans. There is bipartisan support in Congress to make MEPs available to all start-ups and small businesses, and the President will include in his 2017 budget a proposal that would make it easier for employers to use MEPs to create 401(k) plans for their employees.

Today, these businesses face financial and administrative challenges, as well as legal risks, in offering a retirement plan to employees. Allowing small businesses to band together to offer their employees a retirement plan will greatly reduce the number of workers without access to a workplace plan. Given that lifetime income strategies greatly reduce the risk of outliving retirement savings, these plans should be required to make a lifetime income option available to their employees.

IRI agrees with the recommendations put forth in the Senate Finance Committee's Savings and Investment Bipartisan Tax Working Group Report in July 2015. In the report, the Tax Working Group discusses the power of MEPs to enable small employers to sponsor high-quality, low-cost plans. The working group recommends that the Senate Finance Committee consider proposals that will allow all employers to join multiple employer plans, as well as allow businesses to share administrative and other responsibilities associated with providing retirement plans to their employers.

The proposal contained in the President's 2017 Budget would remove the "common bond" requirement for using a MEP, and as a result, would enable employers to

[8] Insured Retirement Institute. *Baby Boomers and Generations Xers: Are They on Track to Reach Their Retirement Goals?*
[9] Insured Retirement Institute. *Boomer Expectations for Retirement 2013.*
[10] Insured Retirement Institute. *Boomer Expectations for Retirement 2011.*
[11] Insured Retirement Institute. *Survey of Americans Aged 51 to 67.*
[12] Insured Retirement Institute. *Tax Policy and Boomer Retirement Saving Behaviors.*

take advantage of "Open MEPs" while adding significant new safeguards to ensure workers are protected. This will allow more small businesses to offer cost-effective, pooled plans to their workers, and certain nonprofits and other intermediaries will be able to create plans for contractors and other self-employed individuals who don't have access to a plan at work. As an added benefit, if an employee moves between employers participating in the same Open MEP, or is an independent contractor participating in a pooled plan using the Open MEP structure, the employee can continue contributing to the same plan after starting work for a different company.

Enable Annuity Portability

In addition to expanding coverage for American workers, we also need to reinvent retirement programs to ensure that workers in an increasingly mobile economy can carry their benefits with them across an entire career. One such effort would be to have Congress amend a technicality in the tax code to make a record keeping change a distributable event for annuities with lifetime income benefits. This change will ensure workers do not lose the lifetime income guarantees they have already paid for if their employer decides to change annuity products or service providers. Unfortunately, to avoid this possibility, many employers simply choose not to offer lifetime income options to their workers. The report's guidance about the issues that occur based on current law that prevent savers from transferring their lifetime income investment to another retirement plan or IRA is a valuable statement of support for our efforts. Lifetime income portability provisions to solve this problem were included in Chairman Hatch's SAFE Retirement Act and the President's budget.

Clarify Employer Fiduciary Responsibility

An increase in workers' access to lifetime income in retirement plans is a crucial step in the advancement of common sense retirement security policies. This will require clear rules for employers to follow about how to select lifetime income products in their retirement plans so that they are confident in meeting their fiduciary responsibilities. Employers do not have the expertise to make the decisions required by current regulations. This can be addressed by allowing employers to select products provided by insurers that meet certain existing regulatory requirements, such as minimum capital and reserving standards. Members of the committee have proposed a safe harbor with respect to the selection of a lifetime retirement income contract as long as certain requirements are met. Such a safe harbor would go a long way towards encouraging more retirement plans to offer lifetime income options.

Increase Auto-Enrollment and Auto-Escalation Default Rates

The Pension Protection Act allows employers to automatically enroll employees in 401(k) plans. Currently the majority of private-sector employees using automatic enrollment set the default rate at 3 percent of pay, the starting point for the auto-enrollment safe harbor. This is too low for adequate retirement savings. Research by EBRI has found that a 6 percent default savings rate would lead to significantly better retirement outcomes for workers without causing a marked increase in workers opting out of the plan. Workers across all income brackets are more likely to participate when their employers have auto-enrollment, but will need higher savings thresholds to reach their retirement savings goals. Starting the deferral rate at 6 percent at the time of automatic enrollment with automatic escalation up to 15 percent would greatly increase retirement savings in the United States. Legislation should be enacted to increase the thresholds. IRI supports the Working Group's recommendation to expand the safe harbor for automatic enrollment plans and provide a new credit to further help small employers offering matching contributions.

In addition, IRI recently submitted a comment letter to the Department of Labor regarding its proposed regulation titled "Savings Arrangements Established by States for Non-Governmental Employees" (29 CFR Part 2510), as published in the Federal Register, Volume 80, No. 222 on November 18, 2015. The proposed regulation would establish a new safe harbor under the Employee Retirement Income Security Act of 1974 (ERISA) for state governments to create and administer automatic enrollment payroll deduction savings arrangements for private-sector employees whose employers do not offer retirement savings plans.

IRI recommended that the Department of Labor address concerns about multiples classes of employers across state lines by directing its efforts to expand coverage on employers rather than providing a path for states to act as plan providers. Specifically, in lieu of the proposed safe harbor for state-run plans, the DOL should simply modify the existing safe harbors referenced above to: (1) Allow all IRA and 403(b) programs and arrangements covered by the existing safe harbors to offer automatic enrollment and automatic escalation features, subject to the requirements already

applicable to automatic features in non-safe harbor plans; and, (2) if desired, clarify that the existing IRA safe harbor is available for IRA programs offered or required under applicable state law so long as participation by individual employees remains voluntary. IRI would strongly urge Congress to consider making the amendments to the existing ERISA safe-harbors referenced above which would contribute greatly to greater use of auto-enrollment and auto-escalation features of IRA's by workers.

Require Lifetime Income Estimates on Workers' Benefit Statements

The Working Group noted that requiring lifetime income disclosures on retirement statements would aid plan participants in making choices about how to spend their savings. To help workers save appropriately for retirement, they need to be aware of how much monthly income their nest egg will generate in retirement. The Department of Labor is working on a rule that would require this information to be included on benefit statements—via lifetime income estimates. Likewise, legislation has been introduced that would also require the inclusion of these estimates on statements. Research by IRI found that more than 90 percent of workers want these estimates and find them helpful. Additionally, more than 75 percent of workers said they would increase their savings level by a few percentage points or more after seeing these retirement income estimates.

Update Required Minimum Distribution (RMD) Rules to Reflect Longer Lifespans

Legislation should be enacted to increase the RMD age from 70½ to at least 75, and mortality tables should be updated to reflect longer life expectancies. The RMD age has been set in stone for more than 50 years. When it was set in 1962, life expectancies were considerably shorter than they are today. Today's workers face an increased risk of outliving retirement assets as a result of longer life spans. Increasing the RMD age will give individuals more time to let their savings grow and allow them to take larger distributions in the future.

Tax Deferral Spurs Retirement Savings

The deferral of taxes on the investment growth within a retirement savings product is one of the cornerstones of retirement planning. The deferral of this growth leads to a larger retirement nest egg for the investor. For example, a 45-year old investor at the 15 percent tax bracket who makes a one time $1,000 contribution before taxes into a tax-deferred retirement account, earning a 6 percent interest rate, will at age 60, have accumulated $2,397 but must pay a 15 percent tax—or $359—upon withdrawing the savings from the account. After taxes, there will be $2,038. If the same investor used after-tax dollars contributed to a taxable account the value of the account at age 60 would be $1,793, or $245 less than the tax deferred savings.[13]

Annuity ownership provides an avenue for many to attain tax-deferred retirement savings growth. More than four in 10 American private-sector workers do not have access to a tax-deferred defined contribution retirement plan through their employer,[14] so annuities provide a vehicle for these workers to access tax-deferred retirement savings.

American consumers place a high-level of importance on tax deferral. Tax deferral is cited by consumers and financial advisors as a top reason for purchasing an annuity.[15] Among middle-income Boomers, 77 percent said that tax deferral is an important consideration when selecting a retirement product.[16]

It is important to note that while the tax-deferred treatment of annuities helps consumers reach a higher level of savings, interest and earnings credited to annuities are taxed when distributions are taken at retirement-taxes on retirement savings and annuities are deferred, not exempt or excluded. Thus, while the removal of annuities' tax—deferred status would not necessarily generate additional tax revenue over the long term, it would have a negative effect on Americans' ability to save for retirement. In fact, a Congressional Budget Office study determined that tax-

[13] *Id.*

[14] Bureau of Labor Statistics. *National Compensation Survey: Employee Benefits in the United States,* March 2013.

[15] Insured Retirement Institute and Cogent Research. *The Evolution of the Annuity Industry, 2012.*

[16] Insured Retirement Institute. *Tax Policy and Middle-Income Boomers.*

deferred retirement savings would moderately increase federal revenues as a percentage of gross domestic product over the long term.[17]

Conclusion

The Savings and Investment Working Group report issued last summer specifically identified three key goals for policy makers to pursue: (1) increasing access to tax deferred retirement savings, (2) increasing participation and levels of savings, and (3) discouraging leakage while promoting lifetime income. IRI strongly supports these goals. The President's budget includes many of the same ideas. Therefore, strong, bipartisan support exists for these proposals, and IRI will continue to work with Congress as the Senate Finance Committee moves forward with legislation to enact these commonsense reforms.

Thank you, again, for the opportunity to present this testimony. We hope you will find it useful, and we would welcome the opportunity to work with the Senate Finance Committee in the future as you consider additional legislative changes to help all Americans attain financial security in retirement.

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Access to Retirement Accounts and Savings Incentives Will Help Americans Prepare for Retirement

Statement for the Record

Pamela Villarreal

Senior Fellow
National Center for Policy Analysis

"Helping Americans Prepare for Retirement: Increasing Access, Participation, and Coverage in Retirement Savings Plans"

United States Senate Committee on Finance

January 28, 2016

Chairman Hatch, Ranking Member Wyden, and members of the committee, thank you for the opportunity to submit written comments about the challenges facing retirement savers today and how to increase access and participation for all workers. I am Pamela Villarreal, a senior fellow at the National Center for Policy Analysis. We are a nonprofit, nonpartisan public policy research organization dedicated to developing and promoting private alternatives to government regulation and control, solving problems by relying on the strength of the competitive, entrepreneurial private sector.

The Obama Administration has made it a goal to increase access to retirement savings accounts for workers whose employers do not provide 401(k) accounts. Consider:

- According to the Department of Labor March 2015 benefits survey, 69 percent of civilian workers had access to a defined benefit or defined contribution retirement plan. Of those workers 77 percent participated. In March 2012, 68 percent of civilian workers had access to a defined benefit or defined contribution plan, with a participation rate of 79 percent.
- When broken between full-time and part-time workers in the March 2015 survey, however, 80 percent of full-time workers had access to a defined benefit or defined contribution plan, compared to 38 percent of part-time workers. Moreover, only half of part-time workers who had access to plans actually participated.

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[17] Congressional Budget Office. *Tax-Deferred Retirement Savings' Long-Term Revenue Projections.*

- But these statistics include only plans offered through employers. According to the Investment Company Institute, in 2013 67 percent of U.S. households had retirement accounts through their employer of through individual IRAs.

While one could argue that the participation rate could be much higher, it does not necessarily mean that *access* is the problem. Between 401(k) plans, SEP plans, traditional and Roth IRA plans and the new *MyRA* accounts, anybody who earns at least the amount in wages that they plan on contributing to a retirement account can start and contribute to some type of retirement savings vehicle. But merely increasing access to retirement accounts does not mean that households will contribute to them. The real question is, with the availability of so many types of accounts, why are workers not saving as much as they should, particularly those with lower incomes?

Social Security crowds out saving. As long as Social Security remains the primary income replacement for some workers when they retire, they have little incentive to save. In essence, it is their "bond" fund, and even if they do set aside a little bit of savings, they are not confident that it really matters much in the future compared to the needs they have in the present.

Lower-income workers are risk adverse, and government policies perpetuate this. Not only do lower income workers save less, they are more risk adverse when they do save. Unfortunately, the *MyRA,* which is designed to be an attractive vehicle for young and lower income savers, relegates them to a Treasury bond fund similar to the Federal Thrift Savings Plan's "G" fund, which is not the ideal choice for a worker with 30 to 40 more years before retirement. Since 1987, the average annual rate of return of the G fund has ranged from 1.89 percent to 5.54 percent, depending on the length of time the bonds are held.

Arguably, there are better options for savers than the *MyRA.* To illustrate this, consider comparisons of a stock or stock/bond index fund to a Treasury bond fund. Comparing the rates of return on four stock funds and the G fund shows that, before adjusting for inflation:

- The Vanguard Windsor II fund, which has been around as long as the FTSP G fund, earned a 9.4 percent annual return on investment from 1987 to 2013. Over the same span of 26 years, the FTSP G Treasury bond fund yielded an annual return on investment of only 5.54 percent.
- Stock funds performed better than the G fund even over shorter time spans; the Vanguard 500 Index and Schwab 1000 Index funds had annual rates of return well above 8 percent from 1994 to 2014.
- Even the Fidelity Asset Manager fund (a mix of 85 percent stocks and 15 percent bonds) yielded an annual return on investment (before inflation) of more than 7 percent over 15 years.

Three stock funds performed better over a shorter time period than the G fund did over a quarter century!

In essence, retirement incentives supported by policymakers often lack product neutrality and are even harmful to some savers.

Tax credits are biased against saving. To add insult to injury, significant tax credits such as the Earned Income Tax credit or the Saver's Credit, which benefit low- to moderate-income workers, are refunded to the individual with no stipulations on how the money is spent. While the Saver's Credit does require an individual to have a retirement account, the money received from the credit can be spent however the individual chooses. In 2014, households that qualified for the Earned Income Tax Credit received an average of $2,400, yet the EITC is not tied to savings incentives in any way, shape or form.

Politicians and policymakers often perpetuate the myth that equity investments are only for the wealthy. About a year ago, 30-year Treasury bond yields hit an all-time low. Yet few policymakers talk about the effect of this on savings, such as the fact that retirees may outlive their money if they can't keep up with inflation. Instead, most of the rhetoric is about how dangerous the stock market is, when it is due for a correction, and the billions "lost" in wealth. Yet, there are many who are *not* wealthy but quietly saving for retirement through regular contributions to equity funds and stocks.

In fact, during the financial crisis of 2008, many faithful retirement account savers pulled money out of equity investments or simply stopped saving altogether. But those who stuck with their equity funds and rode out the crisis were better off. From December 1, 2008 to December 31, 2010:

- A $100 monthly (taxable) contribution to a traditional savings account invested in money market funds would have yielded only $21—a 0.71 percent after-tax return.
- A $100 monthly tax-deferred contribution to a bond index fund would have yielded $140—a 5.39 percent rate of return.
- A $100 monthly tax-deferred contribution to an S&P index fund would have yielded $783—a return of nearly 26 percent.

Economists often argue that since Social Security acts as a bond fund due to its safety and low return on investment, thus those who have little to save should be invested in equity funds to provide balance to their retirement "portfolio."

Possible Solutions

Expand Individual Retirement Accounts (IRAs). Current tax law penalizes those who do not have employer-sponsored savings plans. For example, participants in an employer-sponsored 401(k) plan can contribute up to $18,000 annually, while nonparticipants can contribute only $5,500 to a tax-advantaged IRA. This policy is particularly harmful to early retirees. Level the playing field to treat all savers equally.

Add savings stipulations to tax credits. Rather than send low-income workers a check when they file their tax returns, the federal government could deposit half of each EITC refund into an IRA-type account, similar to auto enrollment in employer plans. Tax filers would still receive half of the credit in cash. Likewise, the Savers' credit could also be deposited into the account.

Expand the MyRA to include other fund options as are available in the Federal Thrift Savings Plan. Or better yet, scrap the MyRA and incorporate some of the features of the MyRA (minimum amount needed to open the account and portability) into universal Roth IRA accounts.

Focus less on creating another retirement account and more on helping those who are unbanked. It is estimated that between 30 and 70 million people do not have a bank account, citing Jack of money, mistrust of banks and high fees for services. While it is not possible to convince everybody to open a bank account if they don't trust banks, it is possible to address high fees. Many experts cite Dodd-Frank, particularly the "Durbin amendment" (imposed price controls on the fee paid by retailers when consumers use a debit card) for the increase in fees and the rise in the number of unbanked and underbanked. Empirical evidence shows that people are more likely to save if they have a bank account, so it is important to address regulatory barriers that deter consumers from having bank accounts.

Thank you for the opportunity to submit these written comments.

WOMEN'S INSTITUTE FOR A SECURE RETIREMENT (WISER)
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U.S. Senate Committee on Finance

Hearing on "Helping Americans Prepare for Retirement: Increasing Access, Participation, and Coverage in Retirement Savings Plans"

January 28, 2016

Testimony for the Record

M. Cindy Hounsell, President

Introduction

We appreciate the opportunity to submit testimony for the record, to ensure that members of the Finance Committee recognize the significant retirement risks women face—particularly the millions of women who are on the cusp of retirement.

WISER is a nonprofit organization that works to help women, educators and policy-makers understand the important issues surrounding women's retirement income. Our primary mission is financial education and capability—providing women with the crucial skills and information they need to avoid poverty in retirement. As the only organization to focus exclusively on the unique financial challenges that women face in retirement, WISER supports women's opportunities to secure adequate re-

tirement income through research, training workshops, educational materials and outreach. WISER and the U.S. Administration on Aging operate the National Education and Resource Center on Women and Retirement Planning.

WISER's testimony will focus primarily on highlighting the challenges women face when it comes to retirement security and the activities WISER undertakes to help women deal with these challenges. We will also summarize the outcomes of a WISER project that showed significant savings outcomes for low-income workers that resulted from combining a simple savings product with savings incentives. The project suggests that the myRA and an expanded and refundable Saver's Tax Credit would boost saving among low-income workers.

Challenges Women Face

It is clear from the data that, no matter how you slice it, American workers are not saving enough for retirement. This issue is compounded for women. For one, women live longer, which means they need more income and their retirement assets have to last longer. Older women are also more likely to have chronic and costly medical conditions and need long-term institutional care. Further, older women are more likely to be single, which puts them at higher risk for poverty. It is at this later stage of life that many women become poor or in the near poor category for the first time in their lives.

Despite needing more retirement assets, women end up having less. Factors that play into this include pay inequity, uneven work histories due to caregiving responsibilities, and a greater likelihood of working part-time where retirement benefits are not offered.

Financial Capability

The reality of today's retirement landscape is do-it-yourself and do it right, or live at or below the edge of poverty in what are supposed to be the golden years. The nature of today's system of individual responsibility demands financial capability. This is WISER's primary area of focus. We focus on women because of the challenges we set forth earlier. Women are in the difficult position of making big decisions while being unable to afford even a small mistake.

Women, along with their male counterparts, tend also to lack basic financial knowledge, which is often the reason for making serious financial mistakes. Women need the best information and opportunity to access information to ensure that they do not make costly decisions; this information should be targeted to women as spouses and caregivers, as well as to women as employees.

Experience and research shows that relevant information and education can have a dramatic impact on financial outcomes. Blanchett and Kaplan find that good financial planning decisions increase retirement income by 29 percent, which is the equivalent of generating 1.82 percent per year of higher returns.[1]

As mentioned earlier, one of WISER's key initiatives is a program administered cooperatively and funded by the Administration on Aging—the **National Education and Resource Center on Women and Retirement Planning.** The AoA/WISER Resource Center's primary goal is to educate the most women we can possibly reach with information that can assist them in their retirement planning. We seek to provide average and low-income women the opportunity to take the first step toward controlling their financial futures.

WISER's approach is to bring financial planning back to the basics. Our goal is to help women make the best decisions they can with the limited resources they may have. We train trainers who assist women in their communities. We explain the hard reality of having to adjust living standards to live within their means and to find resources in their communities that they may not be aware of.

The Center has directly reached tens of thousands of women through our own and our partners' workshops, and we've reached millions with our publications and website. The Center's strength is providing women with core financial knowledge that encourages them to make financial and retirement planning a priority in their lives. We focus on such issues as health and retirement, benefits at work (or the implication of the lack of such benefits), the financial implications of providing care for children, parents and spouses, and the risks of inflation and longevity.

[1] Blanchett, David and Paul Kaplan, *Alpha, Beta . . . and Now Gamma. Measuring the Importance of Intelligent Financial Planning Decisions.* December 18, 2012. *http://www.morningstar.com/advisor/t/68379508/alpha-beta-and-now-gamma.htm.*

We have identified several issues that women are in particular need of learning about or better understanding:

- How much is needed for a secure retirement.
- Longevity risk.
- The value of guaranteed lifetime income.
- How to draw down assets.
- The impact of future inflation and taxes.

It's important to recognize that many women assume they will just keep working beyond normal retirement age. But more than 40 percent of Americans end up retiring earlier than they planned to, usually due to job loss, family needs including caregiving, health issues, or poor personal health.

Appalachian Savings Project

Retirement income security is an elusive goal for low-wage earners. They tend to have no access to 401(k)-type plans, and IRAs are out of reach, with minimum deposits and required automatic payments the norm.

Through WISER's Appalachian Savings Project, we set out to determine the impact on saving of combining easy access to a simple savings vehicle with a matched incentive to save. The project demonstrated that low-income workers are interested in saving and can accumulate significant savings when they are incentivized to do so.

The project established incentives for rural childcare workers to save small amounts with auto-debits for US I-Bonds via *TreasuryDirect,* the U.S. Treasury's online site.[2] Participants received a $50 match to establish an account, and another $50 if they directed at least $50 into their accounts at tax time. Further, the project matched 50 percent of savings after a year of participation (up to $400), simulating an expanded Saver's Credit to measure its effects on savings rates. Quarterly financial workshops were offered to participants, each tailored to the childcare business.

Topics included preparing for tax filings, Social Security, and a legal seminar on wills, power-of-attorney and related subjects.

Among the project findings:

- Participants' total savings including the match averaged $1,150, estimated to be 5.5 percent of their average annual incomes.
- Nearly all respondents agreed that their total savings and investments had increased compared to 12 months earlier.
- Only two respondents reported an increase in debt over the same period.
- Six in 10 respondents reported purchasing savings bonds monthly or more often during the program.
- About one-half used their most recent tax refund to purchase savings bonds.
- The interviewees had generally earmarked their savings bond purchases for longer-term uses, including retirement.

These findings indicate that the savings participants accumulated through the program represented a net increase in savings, rather than a shift in existing resources to savings bonds or increased use of debt in order obtain the match.

The Appalachian Savings Project demonstrated that a low-dollar, easily accessible savings vehicle, combined with a matched incentive to save, produces significant savings by low-wage earners. The 50 percent match provided a clear economic incentive to save. In theory, the Saver's Credit should function in the same way. However, the credit is currently nonrefundable and only applies to contributions to qualified retirement accounts, dramatically limiting the number of households that benefit from it. This project suggests that an expanded and refundable Saver's Tax Credit would support saving by financially vulnerable households.

Historically, a significant gap has existed in the marketplace for a savings product that meets the needs of moderate- and low-income workers; one that does not re-

[2] WISER selected I Bonds because they only have to be held for one year. If the money is withdrawn before 5 years, only one quarter's interest is forfeited. I Bonds have no fees for opening or maintaining an account, have a low minimum contribution, no risk of loss of principal, and inflation protection.

quire a large minimum investment to open the account, is low-risk with low fees, that can be purchased in small increments, is available nationally, and is accessible regardless of credit score.

When the Appalachian Savings Project began, the I-Bond through *TreasuryDirect* was the best savings vehicle available for lower-income savers. Since then, however, the U.S. Department of the Treasury unveiled the MyRA. The design, modeled after a Roth IRA, allows for an initial contribution of as low as $25, and even lower additional contributions. The interest rate is set at the same variable rate as investments in the government securities fund for federal employees and has no fees associated with it. Further, contributions to a MyRA are eligible for the Saver's Credit. Going forward with the Appalachian Savings Project and similar efforts by WISER, MyRA will be the preferred savings vehicle.

Conclusion

Mr. Chairman, thank you for including women's retirement issues as part of the broader discussion on retirement security. As I hope my written testimony has pointed out, women are at a particularly high risk for poverty in retirement. We need to make it easier for people and give them some level of confidence that they can do this, or they just throw their hands in the air and say, "I will never have $2 million so what is the point?" The point is that a little can go a long way and we know that women need confidence to build on their financial knowledge and make better decisions.

There is no single solution to these issues. We need to start understanding what the specific challenges are to certain segments and target those segments with a wide range of solutions from financial education, to guaranteed income product design, policy changes and other innovations.

Most of all, we need to continue to build on what is working and make it better. While there are endless discussions in Washington about what the correct solution is, millions of Americans are just trying to achieve financial stability.

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